United States Court of Appeals
for the Second Circuit

APPENDIX

ORIGINAL

76-7528

United States Court of Appeals

FOR THE SECOND CIRCUIT

B

P/S

UNITED STATES STEEL AND CARNEGIE PENSION FUND, INC., CONNECTICUT MUTUAL LIFE INSURANCE COMPANY, and THE NATIONAL BANK OF COMMERCE OF DALLAS (AS TRUSTEE OF THE OMEGA-ALPHA, INC. POOL TRUST),

Plaintiffs-Appellants,

—against—

HENRY ORENSTEIN, FIRST NATIONAL CITY BANK, HAYDEN STONE INC., BERNSTEIN-MACAULAY, INC., ROGER S. BERLIND, and SANFORD I. WEILL,

Defendants,

—and—

FIRST NATIONAL CITY BANK,

Defendant-Appellee.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

JOINT APPENDIX

Volume I

(Pages A1 to A814)

UNITED STATES COURT OF APPEALS
FILED
JAN 31 1977
A. DANIEL FUSARO, CLERK
SECOND CIRCUIT

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Docket Entries: 74 Civ. 391

CIVIL DOCKET ~~JUDGE WEINFELD~~ 74 CIV. [illegible]

UNITED STATES DISTRICT COURT

C. Form No. 100 Rev. JUDGE KNAPP -23-76

Jury demand date: by pltff.

[redacted]

TITLE OF CASE

-21-75-action consolidated with 72 Civ 3272 for all purposes. Knapp, J.

UNITED STATES STEEL AND CARNEGIE PENSION FUND INC. CONNECTICUT MUTUAL LIFE INSURANCE COMPANY, AND NATIONAL BANK OF COMMERCE OF DALLAS, (AS TRUSTEE OF THE OMEGA-ALPHA, INC. [illegible] TRUST).

vs.

HENRY ORENSTEIN, - Disc. 2-18-76
FIRST NATIONAL CITY BANK, - (Opinion) 7-21-76 - Dismissed
HAYDEN STONE, INC. - Disc. 2-18-76
BERNSTEIN-MACAULAY, INC. - Disc.
ROGER S. BERLIND, AND Disc. 2-18-76.
SANFORD I. WEILL. - Disc. 2-18-76

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For plaintiff:

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Keane & Butler(deft. Orenstein)
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Shearman and Sterling(FNCB)
53 Wall St, NYC 10005 483-1000

STATISTICAL RECORD	COSTS			DATE	NAME OR RECEIPT NO	REC.		DISB.
5 mailed X	Clerk			1/23/74	Bre. of C.	15—		
				1/25/74	U.St.		15—	
6 mailed 7-31-76	Marshal							
sis of Action:	Docket fee							
C. ACT 1933&34								
	Witness fees							
tion arose at:	Depositions							

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Docket Entries: 74 Civ. 391

[illegible]

74 CIV. 3

~~JUDGE WEINFELD~~ JUDGE [illegible]

DATE	PROCEEDINGS	Date Ord. Judgment
Jan23-74	Filed Complaint. Issued Summons.	
Jan23-74	Filed Affidavit of Robert A. Hicks in support of an application to have Thomas P. McCloy, Donald L. Price and Meredith Jane Boylan, appointed to serve the summons and complaint. Burkhardt, Clerk.	
Jan.31-74	Filed summons and affdvt. of service of Thomas P. McCloy	
Feb 1-74	Filed pltffs. first request for production of documents from deft. Roger S. Berlind.	
Feb 1-74	Filed pltffs. first request for production of documents from deft. Hayden Stone Inc.	
Feb 1-74	Filed pltffs first request for the production of documents from deft. First National City Bank.	
Feb.21-74	Filednotice of re-assignment to J. Weinfeld.	
Feb.19-74	Filed pltfs. 1st request for producbion of documents from deft. Sanford Weill.	
Mar.4-74	Filed stip. and order that the time of all defts. to answer complaint is ext. to March 29,1974. So ordered,Weinfeld,J.	
Mar.12-74	Filed deft. Hayden Stone,Inc. answer to pltfs. 1st request for production of documents.	WF&G
Mar.12-74	Filed deft. Sanford I. Weill answer to pltfs. 1st request for production of documents.	WF&G
Mar.15-74	Filed deft. Roger Berlind answer topltfs. 1st request for production of documents.	
Mar.20-74	Filed defts. Hayden Stone,Inc.,Bernstein-Macaulay,Inc.,Roger Berlind and Sanford Weill memorandum in support of motion for consolidation with 72-3272(AB) and 73-4136(MEF).	
Mar.20-74	Filed defts. Hayden Stone,Inc.,Bernstein Macaulay,Inc.,Roger Berlind and Sanford Weill affdt. and notice of motion for an order consolidating actions ret. on: March 27,1974.	
Mar.27-74	Filed stip. and order that the return date on motion by defts. Hayden Stone Inc.,Bernstein Macaulay,Inc.,Roger S. Berlind and Sanford Weill for an order consolidating this action with 72-3272)AB) and 73-4136 MEF) is adj. to April 10,1974 and that all papers in opposition to this motion shall be served on defts. atty. by April 5,1974.So ordered, Bauman,J.	
Apr.2-74	Filed deft. Henry Orenstein notice to take deposition of pltfs. on May 29,30,31, 1974.	
Apr.2-74	Filed deft. HENRY ORENSTEIN ANSWER to complaint.	K&B
Apr.1-74	Filed defts. HAYDEN STONE,INC. AND BERNSTEIN MACAULAY INC. ANSWER to complaint.	WF*G
Apr.1-74	Filed deft. Roger S. Berlind and Sanford Weill ANSWER to complaint.	WF&G
Apr. 1-74	Filed deft. First Natl. City Bank notice to take depostion of pltf. on April 9,1974.	
Apr. 1-74	Filed deft. First Natl. City Bank ANSWER to complaint.	S&S
Apr- 8-74	Filed pltfs' memorandum of law in opposition to motion for consolidation.	
Apr-5-74	Filed defendant Orenstein's request for production of documents.	
Apr. 19-74	Filed defts. Rogers S. Berlind and Sanford I. Weill amended answer to complaint.	WF&G
Apr.19-74	Filed defts. Hayden Stone,Inc, and Bernstein Macaulay,Inc. amended answer to complaint.	
Apr.23-74	Filed copy of order signed by J. Bauman(orig.copy in72-3272AB)--ORDERED that this action be consolidated for thr purpose of all trial proceedings in 72-3272AB and that the motion of defts. Hayden,Bernstein Macaulay,Berlind and Weill for an order consolidating actions for trial is denied without prej. to its renewal. Bauman,J.m/n	

(see Pg. 3)

Docket Entries: 74 Civ. 391

91(M) U.S. Steel, etal vs. Henry Orenstein JUDGE KNAPP 74 Civ 391

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C. 110 Rev. Civil Docket Continuation

DATE	PROCEEDINGS	Date Order or Judgment Noted
ay 3-7	Filed pltfs. notice to take deposition of Leonard Richards on June 11,1974.	
ay 3-74	Filed pltfs. notice to takedeposition of the following: Morton Siegel on June 25,1974 Conrad Sterrett on July 10,1974 Jay Inglis on July 17,1974 Roger Berlind on July 24,1974. Sanford Weill on July 31,1974	
y 3-74	Filed pltfs. notice to take deposition of the following: Sanford Obolsky on June 19,1974 Jack Rose on June 24,1974	
ay 15-74	Filed Interrogatories of Defts. Hayden Stone Inc., Bernstein Macaulay, Inc, Roger S. Berlind and Sanford I. Weill to Pltffs. in action 72 Civ.3272.	
ay 15-74	Filed Interrogatories of Defts. Hayden Stone Inc, Bernstein Macaulay Inc, Roger S. Berlind and Sanford I. Weill to Deft. Henry Orenstein.	
ay 15-74	Filed Interrogatories of Defts. Hayden Stone Inc., Bernstein Macaulay Inc, Roger S. Berlind and Sanford I. Weill to Deft. Arthur Young & Co.	
ay 15-74	Filed Interrogatories of Defts. Hayden Stone Inc, Bernstein Macaulay Inc, Roger S. Berlind and Sanford I. Weill to Pltff U.S. and Carnegie Pension Inc.	
May 15-74	Filed Interrogatories of Defts. Hayden Stone Inc, Bernstein Macaulay Inc, Roger S. Berlind and Sanford I. Weill to Pltff National Bank of Commerce of Dallas	
ay 15-74	Filed Interrogatories of Defts. Hayden Stone Inc, Bernstein Macaulay Inc, Roger S. Berlind and Sanford I. Weill to Deft. First National Bank.	
ay 15-74	Filed for Defts Hayden Stone et al. Request for Production of Documents.	
ay 15-74	Filed for Defts. Hayden Stone Inc. et al. Request for Production of Documents	
ay 15-74	Filed for Defts. Hayden Stone Inc. et al. Request for Production of Documents.	
ay 15-74	Filed for Defts. Hayden Stone Inc. et al. Request for Production of Documents.	
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ay 15-74	Filed for Defts. Hayden Stone Inc. et al. Request for Production of Documents.	
ay 15-74	Filed for Defts. Hayden Stone Inc. et al. Request for Production of Documents.	
ay 15-74	Filed Interrogatories of Defts. Hayden Stone Inc. Bernstein Macaulay Inc, Roger S. Berli and Sanford I. Weill to Pltff Connecticut Mutual Life Ins. Co.	
ay 15-74	Filed Interrogatories of Defts. Hayden Stone Inc, Bernstein Macaulay Inc, Roger S. Berli and Sanford I. Weill to Pltffs. in Action 73 Civ.4136.	
ay 13-74	Filed 1st set of joint interrog. and documents requests to defts. by deft/ 1st Natl. City Bank(also in 72-3272;73-4136MEF;) AB	
y 16-74	Filed pltfs. 1st set of interrog. to deft. 1st Natl. City Bank.	
y 16-74	Filed pltfs. 1st request for production of documents from Henry, Orenstein.	
y 16-74	Filed pltfs. supplementary request for the production of documents from Hayden Stone,Inc.,Rogers Berlind and Sanford Weill.	
y 13-74	Filed 1st set of joint interrog. and document request to US Steel pltfs. of deft. 1st Natl. City Bank(also in 72-3272;AB; 73-4136 MEF & 74-391)	
Jun 3-74	Filed deft. Hayden Stone,Roger Berlind and Sanford Weill response to pltfs. supplementary request for produceation of documents.	
un 6-74	Filed pltfs. US Steel and Carnegie Pension Fund,et al response to the interrog. of deft. FNCB.	
n 5-74	Filed pltfs. US States Steel and Carnegie Pension Fund,Inc. response to defts.Hayden Stone,Inc.,Bernatein Macaulay Inc,Roger Berlind and Snaford Weill interrog.	

(over)

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Docket Entries: 74 Civ. 391

74 Civ. 391 U.S. Steel, etal vs. Henry Orenstein, etal 74 Civ.

JUDGE KNAPP

Page #4

DATE	PROCEEDINGS	Date Ord. Judgment
Jun 5-74	Filed pltf. Natl. Bank of Commerce of Dallas response to the interrog. of defts. Hayden Stone, Bernstein Macaulay, Roger Berlin and Sanford Weill.	
Jun 5-74	Filed pltf. Connecticut Mutual Life Ins. Co. response to defts. Hayden Stone, Bernstein Macaulay Roger Berlind and Sanford Weill Interrog.	
Jun 17-74	Filed stip. and order that the time of defts. (all defts. except Henry Orenstein) to answer each other's interrog. and documents requests is ext. to June 24, 1974. So ordered, Weinfeld, J.	
Jun 19-74	Filed pltfs. affdt. and notice of motion for an order requiring defts. Hayden Stone, Inc., Roger Berlind and Sanford Weill to permit pltfs. to inspect and copy certain documents and awarding pltfs. the reasonable expenses incurred in making this motion including attys. fees. ret. on: June 25, 1974.	
Jun 19-74	Filed memorandum in support of pltfs. motion for an order compelling the production of documents from defts. Hayton Stone, Roger Berlind and Sanford Weill.	
Jun-24-74	Filed defendants Haydon Stone Inc., Berlind and Weill's memorandum in opposition to motion to compel production.	
Jun-24-74	Filed defendants (Haydon, Berlind and Weill) affdvt. of L. Robert Griffin in opposition to pltf's motion to compel.	
Jun-24-74	Filed defendants (Haydon, Berlind and Weill) affdvt. of Anthony F. Phillips in opposition to motion by pltf. to compel.	
Jun-11-74	Filed response of pltf. National Bank of Commerce of Dallas to request for production of documents of defendants Hayden Stone, Inc., Bernstein-Macaulay, Inc., Roger S. Berlind and Sanford Q. Weill.	
Jun-11-74	Filed response of pltf. Conn. Mut. Life Ins. Co. to request for production by defendants'	
Jun-11-74	Filed response of pltf. United/States Steel and Carnegie Pension Fund Inc. to request for production of documents by defendants.	
6/25/74	PRE-TRIAL CONFERENCE HELD BY Mag. Schreiber	
Jul 1-74	Filed stip. and order that the time of defts. 1st Natl. City Bank, Hayden Stone, Bernstein Macaulay, Inc., Roger Berlind and Sanford Weill to answer each other's interrog. and document requests is ext. to July 12, 1974. Soordered, Weinfeld, J.	
Jul 8-74	Filed defts. Hayden Stone, Inc., Roger Berlind and Sanford Weill affdt. and notice of motion for a review by this court on July 16, 1974 in Rm. 905 at 2:15pm of a recommended order signed July 1, 1974 by Mag. Schreiber insofar as the said recommended order directs the production of transcripts of testimony before and a stip. of fact entered into with American Stock Exchange by Hayden Stone with regard to T	
Jun 28-74	Pretrial conference held by Mag. Schreiber.	
Jul-18-74	Filed memo endorsed on pltf's motion filed 6-19-74 - Motion referred to Magistrate Schreiber to hear and report. - Weinfeld, J.	
Jul-18-74	Filed Magistrate Schribers recommended order in re discovery. (signed 7-1-	
Jul-17-74	Filed memo endorsed on defts Hayden Stone et. al.'s motion of objection to Magistrates order: Motion granted without prejudice to the renewal by plaintiff's of their application to obtain access to this information following the depositions of defendants and other person pltf. wish to depose. - Weinfeld, J. m/n	

(see pg. -5-)

Docket Entries: 74 Civ. 391

Civ. 391 US STEEL VS ORENSTEIN, ET AL JUDGE KNAPP ~~WEINFELD~~, J.

PAGE 5

DATE	PROCEEDINGS
Jul 31-74	Filed pltfs. notice to take deposition of Manufacturers Hanover Trust Co. on Aug. 6, 1974. (subpoena issued)
Aug. 1-74	Filed ORDER--ORDERED that defts. permit pltfs. to inspect and copy documents that refer or relate to the following as indicated. Weinfeld J. m/n
7-29-74	PRE-TRIAL CONFERENCE HELD BY Mag Schreiber
Aug. 8-74	Filed verification page of Bernstein-Macaulay, Inc. for answes and objections of defts. Hayden Stone, Inc. and Betnstein Macaulay, Inc. to deft. FNCBank's 1st setof joint interrog. to defts.
Aug. 14-74	Filed response of deft. 1st Natl. City Bank to interrog. of certan defts. with exhibits A through E.
Aug. 14-74	Filed response of deft. 1st Natl. City Bank to interrog. of certain defts. with exhibits F through P.
Aug. 1?-74	Filed response of deft. First Natl. City Bank to interrog. of defts. Hayden Stone Inc., Bernstein-Macaulay, Inc., Roger Berlind and Sanford Weill.
Sep. 4-74	Filedpltfs. notice to take deposition of Peter Bernstein on Aug. 15, 1974.
Sep. 4-76	Filed response of Connell pltfs. to 1st document request of defts. Bernstein Macaulay, Hayden Stone, Roger Belind and Sanford Weill.
Sep. 4-74	Filed pltfs. notice to take deposition of CBWL Hayden Stone on Aug. 14, 1974.
Sep. 4074	Filed pltfs. answers ard objections of connell pltfs. to interrog. of defts. Hayden Stone, Bernstein Macaulay, Berlind and Weill.
Sep. 4-74	Filed response of connell plts. to 1st document requests of deft. 1st Natl. City Bak.
Sep. 4-74	Filed answers and objections of Connell pltfs. to 1st set of interrog. of deft. 1st Natl. City Bank.
Aug. 6-74	Filed answers and objections of defts. Hayden Stone, and Bernstein MacAulay to deft. 1st natl. city bank's 1st set of joint interrog. to defts.
Aug. 6-74	Filed response of defts. Hayden Stone and Bernstein Macaulay to document requests of deft. 1st natl. city bank.
Aug. 6-74	Filed answers and objections of defts. Berlind and Weill to deft. 1st natl. city bank's 1st set ofjoint interrog. to defts.
Aug. 6-74	Filed response of defts. berlind and weill to document requests of 1st ntal. city bank.
Aug. 7-74	Filed responses of deft. Peter Bernstine to 1st st of joint interrog. of deft. 1st Natl. City Bank.
Aug. 7-74	Filed deft. Peter Bernstein affdt. of Frak Kearny of service by mail.
Oct. 8-74	Filed pltfs. notice to take depsistions of the following: Morton Siegel on 10/24/74 Albert Lusk on 10/28/74 David Holzman on 10/30/74 Edward Waldman on 11/1/74 Jack Rose (contd.) on 11/12/74 Sanford Obolsky (contd). on 11/14/74 (subpoenas issued)
[illegible]	PRE-TRIAL CONFERENCE HELD BY Mag Schreiber
[illegible]	PRE-TRIAL CONFERENCE HELD BY Mag Schreiber
Oct. 23-74	Filed pltfs. notice to take deposition of deft. Henry Orenstein on Nov. 18, 1974. (subpoena issued)
Oct. 30-74	Filed pltfs. notice to take deposition of deft. Hayden Stone on Nov. 13, 1974. (subpoena issued)

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D. C. 109 Criminal Continuation Sheet

Docket Entries: 74 Civ. 391

74 Civ 391 US Steel vs Orenstein,etc.

JUDGE KNAPP

DATE	PROCEEDINGS
Oct.29-74	Filed pltfs. notice to take deposition of Ivan Samuels on Nov. 13,1974. (subpoena issued)
Nov.6-74	Filed pltfs. 1set of joint interrog. and documents requests to deft. Hayden Stone,Roger Berlind and Sanford Weill.
Nov 13-74	Filed Pltffs. Notice of Depositions of Henry Clarke Jr. and Roger Schlieder on 12/3/74 @2PM
Nov.21-84	Filed pltfs. notice to take deposition of Frederick Pierce on Nov.29,1974 (subpoena issued)
Nov.27-74	Filed pltfs. notice to take deposition of the following: Erle Zoll on Dec.12,1974 Errol Cook Dec. 16,1974 Robert Richter Dec. 18,1974 Salvatore Botte Dec.19, 1974
Nov.26-74	Filed pltfs. 2nd set of interrog. to deft. 1st Natl. City Bank.
Dec.17-74	Filed order--ORDERED that pltfs. complete the depositions ofall parties and witnesses by Jan.30,1975;all depostions inwhich defts. have previously reserved their right to examine the witness shall be completed by Feb.15,1975; all pre trial discovery shall be complet by March 15,1975; an order be entered incorporating the terms and conditions of paragraphs 1 through 6 above within 5 days after this recommended order is signed by Mag. Schreiber,unless within that time an objecting party moves before J. Weinfeld that the order not be entered.Schreiber,Magistrate. m/n [illegible] to J. Knapp [illegible]
01-17-75	Filed Plfttf's request for admissions (First Set). to deft First National City Bank.)
01-24-75	Filed defts. Hayden Stone Inc., Roger S. Berlind and Sanford I. Weill-responses to pltfs. first set of joint interrog. and document request.
01-2-75	Filed deft. Shearson Hayden notice of deposition of White & Case, Esqs., on 2-20-75
01-21-75	Filed response of deft. First National City Bank to second set of interrog. of pltfs.
02-05-75	Filed affdvt. and notice of motion for deft. Hayden Stone Inc. et. al. for an order extending time to complete pre-trial discovery. to 6-15-75
02-05-75	Filed deft. Arthur Young & Company ANSWERS and Objections to interrog of defts Hayden Stone Inc., Bernstein-Macaulay, Inc., Roger S. Berlind & Sanford I. Weill
02-05-75	Filed defts. Hayden Stone Inc., notice of takeing deposition of parties and dates indicated herewithin
02-11-75	Filed defts. Hayden Stone,Inc. et. al.'s notice of deposition of Julius Schwartz.
02-13-75	Filed defts. Shearson Hayden Stone,Inc., Bernstein-Macaulay,Inc., Roger S. Berlind, and Sanford I. Weill's notice of motion re: leave to assert cross-claims.
02-13-75	Filed defts. Shearson Hayden Stone,Inc.et.at. 's memo. of law in support of motion for leave to assert cross-claims.
02-4-75	PRE-TRIAL CONFERENCE HELD BY Mag. Schreiber
0-2-21-75	Filed reply affidavit of L.Robert Griffin in support of deft's motion for ext. of time to complete pretrial discovery.
02-07-75	ACTION REASSIGNED TO KNAPP,J. with consolidated actions.
02-20-75	Filed deft's (Hayden Stone,etal) affidavit & notice of motion to compell White & Case to comply with subpoena duces tecum ret.3-12-75
02-20-75	Filed deft's memorandum of law in support of his motion ret.3-12-75.
2-20-75	Filed affidavit of R.A.Hicks on behalf of all pltff's in response to mot Re: cross-claims.
02-24-75	Filed pltff's second set of interrogatories to deft.

cont'd on page #7

Docket Entries: 74 Civ. 391

Civ 391 US Steel vs. Orenstein,etal 74 Civ 391

Knapp

D. C. 110 Rev. Civil Docket Continuation Page 7

DATE	PROCEEDINGS	Date Orde Judgment
3-07-75	Filed deft's Hayden Stone,etal affidavit & notice of motion to consolidate with 72 Civ 3272, 73 Civ 4136 & 74 Civ 2426 ret.4-4-75.	
03-07-75	Filed deft's Hayden Stone,etal memorandum of law in support of motion to consolidate ret.4-4-75.	
03-07-75	Filed pltff's affidavit & notice of motion Re: production of documents ret.3-14-75	
03-07-75	Filed pltff's memorandum in support of motion ret.3-14-75.	
2-24-75	PRE-TRIAL CONFERENCE HELD BY Mag. Schreiber	
ar.26-75	Filed pltff's memorandum in oppositon to motions by deft's Hayden Stone to consolidate ret.4-4-75.	
ar.25-75	Filed affidavit of R.B.Fiske,Jr. in opposition to crossclaims against Arthur Young	
Mar.25-75	Filed deft's Arthur Young & Co. memorandum in opposition to motion of Hayden Stone deft's for leave to assert cross-claims against them.	
Mar.26-75	Filed deft's (Arthur Young & Co.) memorandum with respect to motion for consolidation.	
Mar.25-75	Filed affidavit of R.B. Fiske,Jr. in partial opposition to consolidation.	
3-12-75	PRE-TRIAL CONFERENCE HELD BY Magistrate Schreiber	
3-26-75	Filed defts' Hayden Stone Inc, etal Notice to take deposition of Alex Hughes.	
pr.2-75	Filed affidavit of L.R.Griffin in opposition to pltff's motion to consolidate.	
pr.2-75	Filed certain deft's memorandum in opposition to motion to compel production of documents.	
ar.25-75	Filed Stip & order that White & Case shall make available to parties for inspection & copying, during the hours of 9;30 A.M. to 5;30 P.M for a period of 20 days after this stip. is signed by Magistrate Schreiber. The motion of Hayden Stone deft's to compel White & Case to comply fully with the subpoena shall be marked off the calendar. So ordered . Magistrate Schreiber.	
pr.7-75	Filed stip & order that deft. First National City Bank to answer with respect to request for admissions-first set is ext. from 2 17-75 to 4-2-75. Knapp,J.	
4-4-75	Filed transcript of record of proceedings, dated Mag. Schreiber	
4/16/75	Filed Affdvt of Service by William Fontan of true copy of Stipulation&Response to 1st set of pltff's requests for admissions upon Joseph T.Dailey,Breed, Abbott&Morgan on 4/4/75(by hand delivery)	
4/16/75	Filed affdvt of service by mail by Wendy I.Sarney of Stipulation&Response to 1st set of pltff's requests for admissions upon: on 4/9/75 Griffin,Fitzgerald,Fiske,Jr.Last,Tauber,Rowe,Jr.and Mordecai Rosenfeld.	
16/75	Filed -Deft's First National City Bank's Request for Admission of Facts-Set#1(filed in 72 Civ.3272)	
-30-75	Filed Order that subject to such safeguards for confidentiality as the parties may deem appropriate, the deft's shall produce for inspection by counsel for pltff's & deft's jointly all such documents as indicated. Knapp,J.	
05-06-75	Filed affidavit of Robert B. Fiske,Jr. in partial opposition to consolidation. (filed in 72 Civ 3272)	
05-12-75	(Docketed in)Connell pltffs response to deft First Natl City Bank's request for Admission of facts-Set No.1(filed in 72 Civ.3272)	

Docket Entries: 74 Civ. 391

74 Civ 391 US Steel Vs Orenstein, etal

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DATE	PROCEEDINGS	Date Judgm
05-14-75	Filed Memorandum & Order #42411: Deft's (Hayden Stone Deft's have moved for consolidating 4 actions. The decision to consolidate only the Connell Action 72 Civ 3272 & this action for all purposes, So ordered. Knapp, J. m/n	
05-28-75	Filed Stip. & Order re: production of documents pursuant to order dated 4-28-75. Knapp, J.	
05-28-75	Filed affidavit of W.H. Thomas, III, Re: documents.	
05-28-75	Action Reassigned to Knapp, J.	
6/25/75	PRE-TRIAL CONFERENCE HELD BY MAG SCHREIBER	
7/31/75	PRE-TRIAL CONFERENCE HELD BY MAG SCHREIBER	
07-09-75	Filed deft's First National City Bank notice to take deposition of of pltff. Connecticut Mutual Life Insurance. Co.	
7/29/75	PRE-TRIAL CONFERENCE HELD BY Mag Schreiber	
08-28-75	Filed Deft. First National City Bank Notice of taking deposition of pltff. Conn. Mutual Life Insurance Co.	
10-24-75	Filed deposition of Arthur Young & Co. taken on 12-26-74. m/n	
11-10-75	Filed deposition of Arthur Young & Co. taken on 1-13-75.	
11-25-75	Filed continued deposition of Arthur Young & Co. taken by pltff. on 9-19-75.	
12-18-75	Filed deposition of Arthur Young & Co. taken by pltff's on 1-15-75	m/
12-18-75	Filed continued deposition of Arthur Young & Co. taken by pltff's on 1-24-75.	
01-12-76	PRE-TRIAL CONFERENCE HELD BEFORE MAGISTRATE SCHREIBER.	
2-2-76	Filed Order to show cause re: reconsideration of order of 1-27-76, with a stay ret: 2-2-76 at 5PM. Knapp, J.	
2-2-76	Filed pltff.'s memo. of law in support of motion for reconsideration of order.	
01-27-76	Filed Memo-Decision #43782; I am, accordingly, constrained to overrule pltff's objection to the deposition questions at issue. So ordered. Knapp, J. m/n (Filed in 72 Civ 3272)	
02-02-76	Filed Hayden Stone's memorandum in opposition to pltff's motion for reconsideration of order.	
02-05-76	Filed pltff's supplementary request for admissions from deft. H. Orenstein.	
02-25-76	Filed trial memorandum of the Hayden Stone Deft's.	
02-18-76	Filed stip & order that action is discontinued as to U.S. Steel, Carnegie Pension Fund, Connecticut Mutual Life Ins. National Bank of Commerce of Dallas, & Hayden Stone, Bernstein-Macaulay, Roger S. Berlind, & Weill, Henry Orenstein, without prejudice & shall not affect the rights of pltffs against the First National City Bank. Knapp, J. (Filed in 72 Civ 3272)	
03-1-76	Filed pltffs' schedule of exhibits, deposition excerpts, & witnesses to be offered in evidence.	
02-27-76	Filed deposition of Joel Cooper on Aug. 6, 1974.	
02-17-76	Before KNAPP, J. Non-Jury trial begun.	
02-18-76	Trial continued.	
02-19-76	" "	
02-20-76	" "	
02-23-76	" "	
02-24-76	" "	
02-25-76	" "	
03-01-76	" "	
03-02-76	" "	
03-03-76	" " & concluded. Decision Reserved.	

cont'd on page 49

Docket Entries: 74 Civ. 391

[redacted]

D. C. 110 Rev. Civil Docket Continuation Page #9 JUDGE KNAPP

DATE	PROCEEDINGS	Date Order or Judgment
3-03-76	Filed pltff's memorandum in support of their motion for reconsideration of 1-26-76 order.	
3-03-76	Filed pltff's trial memorandum .	
3-12-76	Filed Deposition of Arthur Young taken by pltff's on 1-3-75.	
3-12-76	Filed continued deposition of Arthur Young taken on 1-8-75.	
4-06-76	Filed pltff's post trial memorandum.	
04-05-76	Filed pltff's U.S.Steel,etal findings of fact .	
-04-76	Filed Opinion # 44918.Accordingly pltff's. complaints are dismissed. Let deft. submit judgement on five (5) days notice. MN KNAPP J.	
21-76	Filed Judgment: Ordered that pltff's Herein take nothing that action be dismissed with prejudice on the merits as to deft. Citibank N.A.(formerly know as First National City Bank(& that deft. recove its costs of action to be taxed from pltff's. Knapp,J. Judgment Ent. Clerk. Mailed notice. Ent.9-22-76.	
0-19-76	Filed notice of appeal by Pltff U.S. Steel & Carnegie Pension Fund to the U.S.C.A. from Judgment entered 09-21-76 . mailed notice.	
0-29-76	Filed Undertaking for Costs on Appeal by Fireman's Fund-National Surety Corp. in the amount of $250.00 .	
12-16-76	Filed stipulation designating exhibits to be included in the record on appeal.	
12-16-76	Filed stipulation allowing copies of certain missing original documents to be included in the record on appeal.	
12-16-76	Filed stipulation identifying original papers contained in other case files but which are to be included in the record on appeal.	

Docket Entries in the Connell action: 72 Civ. 3272

idated for pre-trial only w/ 73 Civ.4136 & 74 Civ.391.

CIVIL DOCKET

UNITED STATES DISTRICT COURT

C. Form No. 106 Rev.

JUDGE KNAPP

~~JUDGE DUFFY~~ ~~JUDGE~~ [illegible]

Jury demand date: ~~[illegible]~~ Pltff-10-02-75

72 CIV. 3272

TITLE OF CASE

ATTORNEYS

4-75-Action consolidated with 74 Civ 391 for all purposes. Knapp, J.

LESTER CONNELL, et al – 5-05-76 Dis

vs

BERNSTEIN-MACAULAY, INC and – 2-18-76

CBWL-HAYDEN STONE, INC. – 2-18-76

Apr. 22-74

ROGER S. BERLIND, – 2-18-76 Disc

SANFORD I. WEILL, – 2-18-76

PETER L. BERNSTEIN & – 5-5-76

FIRST NATIONAL CITY BANK [illegible] 7-21-76 Disc

For plaintiff:

JACK LAST
11 EAST 44th STREET
NEW YORK, N.Y. 10017
Tel: 682-5514

For Deft: Shearman&Sterling
53 Wall St. NY 10005 483-1000
(Deft. First Natl Bank)

For defendant:

WILLKIE FARR & GALLAGHER
1 CHASE MANHATTAN PLAZA
NEW YORK, N.Y. 10005
TEL; 248-1000

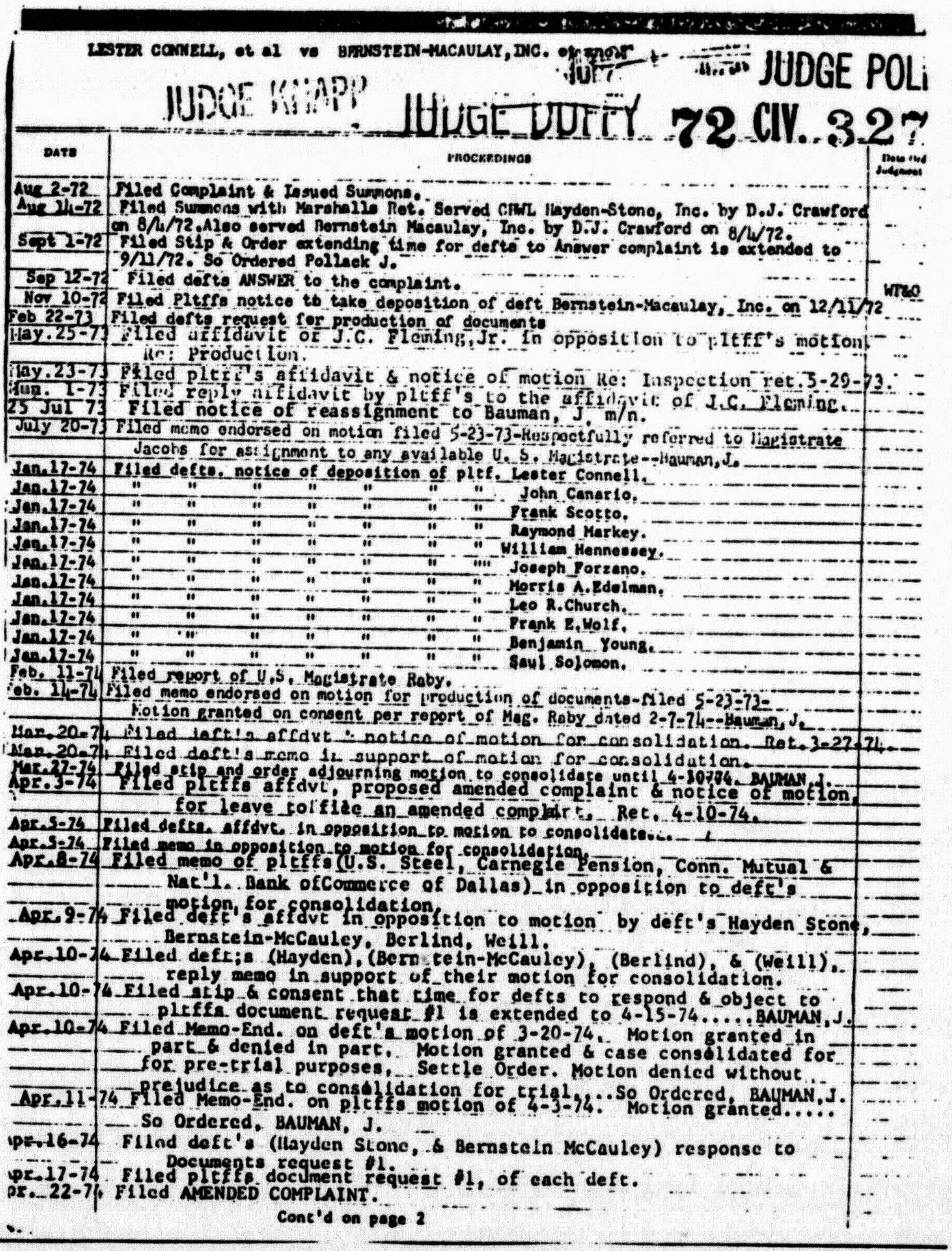
Fulton Walter & Duncombe (Peter L. Bernstein)
30 Rockefeller Plaza, NYC 10020 JU-6-0700

~~Sherman & Sterling (1st. National City Bk)~~
~~53 Wall St. NYC. 10005 483-1000~~ See above

Keane&Butler
200 Park Ave. NY, NY 10017
(Deft. Hentyy Orenstein)

STATISTICAL RECORD	COSTS			DATE	NAME OR RECEIPT NO.	REC.		DISB.
5 mailed X	Clerk			5/2/72	J. Last	15		
				5/4/72	[illegible]		15	
6 mailed 7-21-76	Marshal							
sis of Action: S.E.C. $250,000.00	Docket fee							
	Witness fees							
tion arose at:	Depositions							

Docket Entries in the Connell action: 72 Civ. 3272



LESTER CONNELL, et al vs BERNSTEIN-MACAULAY, INC. et ano

JUDGE KNAPP ~~JUDGE DUFFY~~ JUDGE POL

72 CIV. 327

DATE	PROCEEDINGS	Date Ord Judgment
Aug 2-72	Filed Complaint & Issued Summons.	
Aug 14-72	Filed Summons with Marshalls Ret. Served CHWL Hayden-Stone, Inc. by D.J. Crawford on 8/4/72. Also served Bernstein Macaulay, Inc. by D.J. Crawford on 8/4/72.	
Sept 1-72	Filed Stip & Order extending time for defts to Answer complaint is extended to 9/11/72. So Ordered Pollack J.	
Sep 12-72	Filed defts ANSWER to the complaint.	
Nov 10-72	Filed Pltffs notice tb take deposition of deft Bernstein-Macaulay, Inc. on 12/11/72	WT&O
Feb 22-73	Filed defts request for production of documents	
May.25-73	Filed affidavit of J.C. Fleming, Jr. in opposition to pltff's motion Re: Production.	
May.23-73	Filed pltff's affidavit & notice of motion Re: Inspection ret. 5-29-73.	
Jun. 1-73	Filed reply affidavit by pltff's to the affidavit of J.C. Fleming.	
25 Jul 73	Filed notice of reassignment to Bauman, J. m/n.	
July 20-73	Filed memo endorsed on motion filed 5-23-73-Respectfully referred to Magistrate Jacobs for assignment to any available U. S. Magistrate--Bauman, J.	
Jan.17-74	Filed defts. notice of deposition of pltf. Lester Connell.	
Jan.17-74	" " " " " " " John Canario.	
Jan.17-74	" " " " " " " Frank Scotto.	
Jan.17-74	" " " " " " " Raymond Markey.	
Jan.17-74	" " " " " " " William Hennessey.	
Jan.17-74	" " " " " " "" Joseph Forzano.	
Jan.17-74	" " " " " " " Morris A. Edelman.	
Jan.17-74	" " " " " " " Leo R. Church.	
Jan.17-74	" " " " " " " Frank E. Wolf.	
Jan.17-74	" " " " " " " Benjamin Young.	
Jan.17-74	" " " " " " " Saul Solomon.	
Feb. 11-74	Filed report of U.S. Magistrate Raby.	
Feb. 14-74	Filed memo endorsed on motion for production of documents-filed 5-23-73- Motion granted on consent per report of Mag. Raby dated 2-7-74--Bauman, J.	
Mar. 20-74	Filed deft's affdvt & notice of motion for consolidation. Ret. 3-27-74.	
Mar. 20-74	Filed deft's memo in support of motion for consolidation.	
Mar. 27-74	Filed stip and order adjourning motion to consolidate until 4-10-74. BAUMAN, J.	
Apr. 3-74	Filed pltffs affdvt, proposed amended complaint & notice of motion, for leave to file an amended complaint, Ret. 4-10-74.	
Apr. 5-74	Filed defts. affdvt. in opposition to motion to consolidate....	
Apr. 5-74	Filed memo in opposition to motion for consolidation.	
Apr. 8-74	Filed memo of pltffs (U.S. Steel, Carnegie Pension, Conn. Mutual & Nat'l. Bank of Commerce of Dallas) in opposition to deft's motion for consolidation.	
Apr. 9-74	Filed deft's affdvt in opposition to motion by deft's Hayden Stone, Bernstein-McCauley, Berlind, Weill.	
Apr. 10-74	Filed deft;s (Hayden), (Bernstein-McCauley), (Berlind), & (Weill), reply memo in support of their motion for consolidation.	
Apr. 10-74	Filed stip & consent that time for defts to respond & object to pltffs document request #1 is extended to 4-15-74.....BAUMAN, J.	
Apr. 10-74	Filed Memo-End. on deft's motion of 3-20-74. Motion granted in part & denied in part. Motion granted & case consolidated for for pre-trial purposes. Settle Order. Motion denied without prejudice as to consolidation for trial....So Ordered, BAUMAN, J.	
Apr. 11-74	Filed Memo-End. on pltffs motion of 4-3-74. Motion granted..... So Ordered, BAUMAN, J.	
Apr. 16-74	Filed deft's (Hayden Stone, & Bernstein McCauley) response to Documents request #1.	
Apr. 17-74	Filed pltffs document request #1, of each deft.	
Apr. 22-74	Filed AMENDED COMPLAINT.	

Cont'd on page 2

Docket Entries in the Connell action: 72 Civ. 3272

[redacted]

CONNELL, et al -v- BERNSTEIN-MACAULAY **JUDGE KNAPP** ~~BAUMAN, J.~~

D. C. 110 Rev. Civil Docket Continuation Page 2

DATE	PROCEEDINGS	Do Judg
Apr. 23-74	Filed Order consolidating this action with 73 Civ. 4136 MEF & 74 Civ. 391 EW for pretrial only. BAUMAN, J.	
Apr. 22-74	Filed ANSWER to complaint by Bernstein Macaulay and Hayden Stone.	WF6
Apr. 22-74	Filed ANSWER to complaint by Berlind and Wiell.	WF6
May 2-74	Filed notice of appearance by Fulton Walter & Duncombe for deft. Peter L. Bernstein.	
May 3-74	Filed pltfs. notice of deposition of Leonard Richards.	
May 8-74	Filed ANSWER to complaint by First National City Bank.	S6
May 10-74	Filed pltfs. request for production of documents. (No. 2)	
May 13-74	Filed first set of joint interrogatories and document requests to defts. by deft. First National City Bank.	
May 13-74	Filed first set of joint interrogatories and document requests to Taylor Pltf. of deft. First National City Bank.	
May 14-74	Filed summons with marshals return Served Roger Berlind by Cassidy 4-25-74 Sanford Weill by cassidy 4-26-74. Peter Bernstein by P/S 4-17-74 & First National City Bank by Redding 4-17-74.	
May 14-74	Filed ANSWER to complaint by Peter L. Bernstein.	PO
May 15-74	Filed defts. request for production of documents of Connecticut Mutual Life.	
May 15-74	" " " " " " " " United States Steel.	
May 15-74	" " " " " " " " Henry Orenstein.	
May 15-74	" " " " " " " " First National City Bank.	
May 15-74	" " " " " " " " Arthur Young & Co.	
May 15-74	" " " " " " " " of Pltfs.	
May 15-74	" " " " " " " " Of pltfs. in 73 Civ. 4136.	
May 15-74	" " " " " " " " National Bank of Commerce.	
May 15-74	Filed defts. interrogatories address to deft. Henry Orenstein.	
May 15-74	Filed defts. interrogatories addressed to Arthur Young & Co.	
May 15-74	Filed defts. interrogatories addressed to pltfs U.S.& Carnegie Pension.	
May 15-74	Filed defts. interrogatories addressed to National Bank of Commerce.	
May 15-74	Filed defts. interrogatories addressed to First National City Bank.	
May 15-74	Filed defts. interrogatories addressed to Pltf in 72 Civ. 3272.	
May 15-74	Filed defts. interrogatories addressed to Connecticut Mutual Life.	
May 15-74	Filed defts. interrogatories addressed to pltfs. in action 73 Civ. 4136.	
Jun. 26-74	Filed deft's H. Orenstein answers to first set of joint interrogs. by deft. First National City Bank.	
Jun. 26-74	Filed deft's Berlind & Weill response to pltff's document Request, NO. 2.	
Jul. 10-74	Filed stip & order that time for pltff. etal to answer interrogs. of deft. First National City Bank is ext. to 7-12-74.	
Jun. 27-74	Filed stip & order that time for deft. First National City Bank, etal, to answer to each other's interrogs is ext. from 6-24-74 to 7-12-74. So ordered. Knapp, J.	
6/25/74	Pre-trial Conf. before Mag. Schreiber	
6/28/74	PRE-TRIAL CONFERENCE HELD BY Mag. Schreiber	
Aug. 6-74	Filed Defts Haydon Stone Inc. & Bernstein-Macaulay, Inc. response to document requests of Deft First National City Bank.	
Aug. 6-74	Filed Answers&Objections of Defts Roger S. Berlind&Sanford I. Weill to Deft. First National City Bank 1stset of joint interrogs to Deft.	
Aug. 6-74	Filed Response of DeftsRoger S. Berlind&Sanford I. Weill to document requests of First National City Bank.	
Aug. 6-74	Filed Answers&Objections of Defts Hayden-Stone Inc/Bernstein-MacCaulay, Inc. to Deft. First National City Bank 1st set of joint interrogs to defts.	
7/24/74	PRE-TRIAL [illegible] HELD BY Mag. Schreiber	

(contd pg 3)

Docket Entries in the Connell action: 72 Civ. 3272

LESTER CONNELL ET AL vs. BERNSTEIN-MACAULAY, INC. ET ANO
72 Civ. 3272

(Page 3)

DATE	PROCEEDINGS	Date Ord Judgment
Aug. 7-74	Filed Deft Peter L. Bernstein to first set of Joint Interrogs of deft. First National City Bank	
Aug. 7 74	Filed Deft. Peter L. Bernstein's Affdvt of Service by Mail of Frank P. Kearney on Robert Griffin et al on Aug. 2, 74	
Aug. 8-74	Filed Defts. Hayden Stone Inc. et al Answers&objections to Deft. 1st National City Bank's 1st set of joint interrogs to defts.	
Aug. 13-74	Filed Response of Deft. 1st National City Bank to interrogs of defts Hayden Stone, Inc. Bernstein-Macaulay, Inc. Roger S. Berlind&Sanford I. Weill	
Aug 1[illegible]	Filed Response of Connell Pltffs to 1st Document request of defts. Bernstein-Macaulay Inc. Hayden Stone Inc. Roger S. Berlind&Sanford Weill	
Aug 1[illegible]	Filed Pltff's Notice of taking deposition of Peter L. Bernstein.	
Aug. 19-7[illegible]	Filed Answers & objections of Connell pltffs to 1st Interrogs of Defts Hayden Stone Inc. Bernstein-Macaulay, Inc. Roger S. Berlind&Sanford I. Weill.	
Aug. 19-7[illegible]	Filed Response of Connell pltffs to 1st document requests of deft. First National City Bank.	
Aug. 19-74	Filed Answers&Objections of Connell Pltffs to 1st set of interrogs of deft. First National City Bank.	
Aug. 1[illegible]	Filed Pltffs Notice of taking deposition of Richard [illegible].	
Aug. 20-7[illegible]	Filed Order. Exams before trial of [illegible] Aug 13 Berlind&Weill on [illegible]/5, 16 Oct. 10&22/74. Magistrate Schreiber	
Aug. 16-74	Filed response of deft. First Nat'l City Bank to interrogs of certain deft's.	
Aug. 16-74	Filed response of deft. First Nat'l City Bank to interrogs of certain deft's.	
Oct. 18-74	PRE-TRIAL CONFERENCE HELD BY Mag. Schreiber	
Nov. 1-74	" " " " " " "	
Dec. 17-74	Filed Recommended Order that pltff's complete the depositions of all parties & witnesses by 1-30-75. etc. All pretrial discovery be completed by 3-15-75 & action be ready for trial on that date. Magistrate Schreiber.	
Jan. 20/75	Filed defts. Shearson HaydenStone Inc., Bernstein-Macaulay, Inc., R. Berlind and S. Weill notice to take deposition of White & Case, etc.	
Feb. 5-75	Filed certains deft's affidavit & notice of motion extending time to complete pre-trial discovery ret. 2-24-75 before Magistrate Schreiber. (This copy of motion sent to Judge Knapp's chambers) [illegible]	
02-05-75	Filed defts. Hayden Stone, Inc., Bernstein-Macaulay, Inc., Roger S. Berlind and Sanford I. Weill's notice to take depositions of L. Connell, J. Canario, M. Edelman, W. Hennessey, F. Scotto, B. Young, W. Taylor, W. Abelow, H. Bluestone, D. Goldberg, N. M Metzger, L. David.	
02-05-75	Filed Answers and Objections of deft. Arthur Young & Co. to interrogs. of defts. Hayden Stone, Inc. Bernstein-Macaulay, Inc., Roger S. Berlind and Sanford I. Weill.	
2-11-75	Filed defts. Shearson Hayden Stone, Inc. Bernstein-Maculay, Inc. Roger S. Berlind, and Sanford I. Weill 's noticeto take deposition ofJulius Schwartz.	
02-4-75	PRE-TRIAL CONFERENCE HELD BY Magistrate Schreiber	
2-21-75	Filed reply affidavit of L. Robert Griffin support of motion for extension of time Re: pretrial discovery.	
02-07-75	Action reassigned to Knapp, J.	

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Docket Entries in the Connell action: 72 Civ. 3272

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D. C. 110 Rev. Civil Docket Continuation Page #4 JUDGE KNAPP

DATE	PROCEEDINGS	Init Judg
2-20-75	Filed deft's (Hayden Stone, etal) affidavit & notice of motion compelling White & Case to comply fully with subpoena duces tecum. ret. 3-12-75.	
02-20-75	Filed deft's memorandum of law in support of motion ret. 3-12-75.	
02-24-75	Filed deft's (Shearson Hayden Stone, Bernstein-Macaulay, R.S. Berlind & S.L. Weill) affidavit & notice of motion to serve & file certain cross-claims ret. 3-14-75.	
02-24-75	Filed deft's memorandum in support of motion ret. 3-14-75.	
03-03-75	Filed deft's (Peter L. Bernstein) affidavit & notice of motion to file certain cross claims ret. 3-7-75.	
03-03-75	Filed deft's memorandum in support of motion ret. 3-7-75.	
03-03-75	Filed deft's (Peter L. Bernstein) certificate of service of motion.	
3-07-75	Filed deft. Hayden Stone, etal affidavit & notice of motion to consolidate with 74 Civ 2426 ret. 4-4-75.	
03-07-75	Filed deft. Hayden Stone etal memorandum of law in support of motion, ret. 4-4-75.	
03-11-75	Filed affidavit by Jack Last in opposition to deft's motion re: subpoena duces tecum.	
03-25-75	Filed deft's (Arthur Young & Co's) memorandum with respect to motion for consolidation.	
03-25-75	Filed defts (Arthur Young & Co's) memorandum in opposition to Hayden Stone deft's for leave to assert cross-claims.	
03-25-75	Filed affidavit of R.B. Fiske, Jr. in opposition to cross-claims against Arthur Young.	
03-25-75	Filed affidavit of R.B. Fiske, Jr. in partial opposition to consolidatio	
03-26-75	Filed Defts' (Hayden Stone Inc. et al) notice of deposition, of Alex Hughes.	
04-1-75	Filed pltff's memorandum in opposition to deft's Hayden Stone motion for leave to assert cross-claims & consolidate for trial.	
04-02-75	Filed Reply memorandum of Hayden Stone Deft's in support of motions for leave to assert cross-claims & for consolidation.	
03-25-75	Filed stip & order that White & Case shall make availabe to parties for inspection & copying, during the hours of 9;30 to 5;30 P.M. for a period of 20 days after this stip. is signed by Magistrate Schreiber. The motion of The Hayden Stone deft's to compel White & Case to comply fully the subpoena shall be marked off the calendar. So ordered. Magistrate Schreiber.	
4-4-75	Filed transcript of record of proceedings, dated Mag Schreiber	
04-16-75	Filed Deft First National City Bank's Request for Admission of Facts-Set.#1 (also docketed in 74 Civ.391)	
06-06-75	Filed affidavit of Robert B. Fiske, Jr. in partial opposition to consolidation.	
05-12-75	Filed Connell Pltffs response to deft. 1st Natl. City Bank's Request for Admission of facts. Set No.1	
05-13-75	Filed deft. Hayden Stone's affdvt: further support of motion to compel White & Case with a subpoena duces tecum dated 1-30-75.	
05-14-75	Filed Memorandum & order #42411; Deft's (Hayden Stone Deft's) have moved for consolidating 4 actions. The decision to consolidate only the Connell action & U.S. Steel cases 74 Civ 391 for all purposes. So ordered. Knapp, J. m/n	
05-28-75	Filed deft's Shearson-Hayden Stone, etal affidavit & notice of motion for summary judgment ret. 6-6-75.	
05-28-75	Filed deft's (H. Stone) memorandum in support of motion ret. 6-6-75.	
05-28-75	Filed " " statement pursuant to rule 9(g).	

Docket Entries in the _Connell_ *action: 72 Civ. 3272*

[redacted]

72 Civ 3272 Lester Connell,etal, vs. Bernstein-Macaulay,etal 72 Ci.

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DATE	PROCEEDINGS	Date O. Judgme
05-30-75	Filed pltff's United States Steel & Carnegie Pension Fund affidavits & notice of motion for an order modifying subpoena duces tecum ret. before Magistrate Schreiber on 6-10-75.	
05-30-75	Filed pltff's memorandum of law in support of motion ret. 6-10-75.	
06-09-75	Filed Memorandum of Hayden Stone deft's in opposition to pltff's motion to modify subpoena duces tecum.	
06-06-75	Filed stip & order that time for pltffs to respond to deft's motion for partial summary judgment is ext. from 6-3-75 to 6-20-75. Knapp,J.	
06-17-75	Filed Affdvts of Mole,Thompson,Hook&Jaynes in opposition to Hayden Stone Defts'motion for partial summary judgment.	
06-17-75	Filed Affdvt of R.A.Bicks in opposition to motion of Hayden Stone defts for partial summary judgment dismissing Count IV of complaint in 74 Civ.391	
06-17-75	Filed Memorandum of Law in opposition to Hayden Stone Defts'motion for partial summary judgment.	
06-17-75	Filed Pltffs' statement re:above.	
06-23-75	Filed Memo-endorsed on deft's Hayden Stone etal motion filed 5-28-75 Re: summary judgment. The motion is accordingly denied. Knapp,J.	m/n
07-07-75	Filed Haden Stone deft's notice of motion for reargument ret.before Knapp,J.	
07-07-75	Filed deft's memorandum in support of motion for reargument.	
07-10-75	Filed Memo-endorsed on Hayden Stone deft's motion filed 7-7-75 for reargument: Motion referred to Magistrate Schreiber to hear & report. So ordered. Knapp,J.	
6/26/75	PRE-TRIAL CONFERENCE HELD BY MAG SCHREIBER	
7/8/75	PRE-TRIAL CONFERENCE HELD BY Mag Schreiber	
07-07-75	Filed deft's H. Orenstein first set of Interrogs to pltff. U.S.Steel	
07-09-75	Filed pltff's notice to take deposition of James Ledbetter.	
07-25-75	Filed Defts.Shearson Hayden Stone Inc.et al notice to take deposition of John M. Gray.	
07-25-75	Filed Defts " " " " " " " " " " Wm.H.Tinsley.	
07-16-75	Filed Pltffs Response to 1st set of interrogs of deft.Henry Orenstein.	
7/28/75	PRE-TRIAL CONFERENCE HELD BY Mag Schreiber	
08-12-75	Filed pltffs. U.S. Steel and Carnegie Pension Fund Inc. affdvt. In support of issuance of a subpoena duces tecum.	
08-13-75	Filed pltffs.'notice of deposition of of James Ledbetter.	
08-26-75	Filed deft's First National City Bank's supplementary request for the production of documents from the U.S.Steel & Carnegie.	
09-02-75	Filed pltffs.' request for admissions from Citibank.	
09-02-75	Filed pltffs.' request for admissions from the Hayden Stone defts.	
09-05-75	Filed " notice to take deposition of John Sieff.	
09-09-75	Filed pltff's request for admissions from deft. Henry Orenstein.	
09-18-75	Filed pltff's filing pursuant to order of Magistrate Schreiber.	
09-17-75	Filed Hayden Stone etal notice to take deposition of Ford Motor Credit C	
09-16-75	Filed deft's(Citibank) second set of interrogs to pltff. Connecticut Mutual Life Ins. Co.	
9-19-75	Filed response of pltff. U.S. Steel and Carnegie Pension Fund,Inc. to "First National City Bank's Suppl. request for the production of documents."	
9-23-75	Filed cross-claims of Hayden Stone defts.	WF&G
10-03-75	Filed Deft&Cross Claimant Bernstein:	FWAD
0-02-75	Filed " Henry Orenstein ANSWER to Cross-Claims of Deft.Peter L.Bernstein &Jury trial demanded.	K&B
0-03-75	Filed Cross Claims of Deft.First Natl City Bank.	S&S

(cont PR.6)

Docket Entries in the Connell action: 72 Civ. 3272

72 Civ.3272 LESTER CONNELL ET AL VS. BERNSTEIN-MACAULAY,INC. ET AL

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DATE	PROCEEDINGS	Date O Judgm
10-03-75	Filed ANSWER of Deft.First National City Bank to Cross-Claims of Hayden Stone, Defts.	S&S
10-03-75	Filed ANSWER of " First National City Bank to Cross-Claims of Peter L.Bernstein	S&S
10-03-75	Filed Response of Pltff Conn.Mutual Life Insurance Company to 2nd set of Interrogs of Deft.First National City Bank	
10 10 75	Filed deposition of W.H. Tinsley taken on 8-06-75.(Filed 9-24-75)	
10-10-75	Filed deposition of J.M. Grey taken on 8-06-75. (Filed 9-24-75)	
10-10-75	Filed depoistion of Roger A. Schlieder. m/n	
10- 02-75	Filed Deposition of James F.Ledbetter on 8/11/75.	
10- 07-75	Filed Deft Hayden Stone affdvt&Notice of Motion for an order requiring representative of pltffs,Mr.Harvey Mole ,answer certain questions propounded to him at an oral exam,etc. ret.10/28/75 before Mag.Schreiber,Room 127,4:00 p.m.	
10-17-75	Filed Memorandum of Hayden Stone defts in support of motion to compel answers to questions propounded at oral exam.	
10-24-75	Filed affidavit of R.A. Bicks in opposition to motion by Hayden Stone deft's to compel testimony.	
10-24-75	Filed pltff's memorandum in opposition to motion by Hayder Stone deft's to compel testimony.	
10-24-75	Filed pltff's copy of notice of recommended order by Magistrate Schreiber, on 9-24-75.	
10-24-75	Filed pltff's copy of notice of recommended order by Magistrate Schreiber on 10-21-75.	
10-22-75	Filed Pltff's revised request for admissions from the Hayden Stone deft's.	
10-22-75	Filed ANSWER of deft's Shearson Hayden Stone & Bernstein-Macauley to cross-claims of deft. First National City Bank.	
10-22-75	Filed ANSWER of deft's Roger S. Berlind & Sanford I. Weill to cross-claims of deft. First National City Bank.	
10-23-75	Filed deposition of John Sieff taken on 9-26-75. m/n	
11-06-75	Filed stip & order that the documents annexed to this stip & marked for identification in lieu of a deposition are true & correct copies of the original documents as indicated. Knapp,J.	
11-05-75	Filed pltff's revised request for admissions from Citibank.	
11-06-75	Filed response of deft. Henry Orenstein to revised request for admissions of pltff's.	
11-06-75	Filed First National City Bank'sresponse to pltff's revised request for admissions.	
11-08-75	Filed response of Hayden Stone Deft's to pltff's revised request for admissions.	
11-07-75	Filed Requests to admit of the Hayden Stone deft's to pltff's U.S. Steel etal & pltff's in Lester Connell,etal.	
11-10-75	Filed response of pltff. Connecticut Mutual Life Ins. Co. to deft' First National City Bank's supplementary questions to its 2nd set of interrogs.	
11-11-75	Filed deft.Henry Orenstein affidavit & notice of motion to sever & try separately from actions from other claims ret.11-21-75.	
11-11-75	Filed deft's memorandum of law in support of his motion ret.11-21-75.	
11.19 75	Filed pltff's memorandum in response to motion by deft. H.Orenstein for severance.	
11-19-75	Filed memorandum of hayden Stone deft's in opposition to motion of Henry Orenstein.	
11-19-75	Filed affidavit of Louis A. Craco in opposition to motion of Henry Orenstein.	

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Docket Entries in the Connell action: 72 Civ. 3272

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DATE	PROCEEDINGS	Date O Judgme.
11-11-75	Filed Hayden Stone deft's notice of following corrections to be made in pages 3,4,5 & 6 to pltff's revised requast for admissions.	
11-11-75	Filed deft's Citibank's request for admissions from pltff's.	
11-21-75	Filed deft's " supplementary request for admissions.	
11-25-75	Filed deposition of Ralph Pompea taken on 9-29,& 30,1975.	
11-25-75	Filed response of pltff's to requests for admissions by deft. First Nat'l City Bank.	
11-25-75	Filed response of pltff's to requests for admissions by the Hayden Stone defts.	
11-24-75	Filed pltff's request for admissions from S.I.Weill.	
11-24-75	Filed pltff's request for admissions from P.L.Bernstein.	
11-24-75	Filed pltff's request for admissions from Bernstein-Macaulay, Inc.	
11-24-75	Filed Pltff's request for admissions from Roger S.Berlind.	
11-24-75	Filed pltff's request for admissions from CBWL-Hayden Stone.	
12-02-75	Filed pltff's supplementary response to requests of deft. Citibank.	
12-03-75	Filed " " request for admissions from Hayden Stone Defts.	
12-03-75	Filed " " " " " ! Deft.Citibank	
12-03-75	Filed " Revised request for " " " Henry Orenstein	
12-09-75	Filed Response of Connell Pltffs to request for admissions of The Hayden Stone Defts.	
12-10-85	**Filed response of deft. Peter L. Bernstein to requests for admissions by the Connell pltffs.**	
12-17-75	Filed Deft,Haydon Stone Affdvt&Notice of motion for reargument ret.12/19/75.	
12-17-75	Filed Memorandum of HaydenStone Defts in support of motion for reargument and in opposition to proposed order dated 12/12/75 submitted by various parties.	
12-19-75	Filed deft's Shearson Hayden Stone affidavit & notice of motion to answer certain questions ret.1-9-76.	
12-19-75	Filed deft's memorandum in support of their motion ret.1-9-76.	
12-29-75	Filed deft. H.Orenstein memorandum of law in reply to motion of Hayden Stone deft's for reargument.	
1-06-76	Filed Hayden Stone deft's memorandum of law in support of First Nat'l City Bank's motion Re: production.	
1-06-76	Filed Deft Citibank's revised request for admissions from pltff's.	
01-06-76	Filed First Nat'l City Bank's response to pltff's supplementary request for admissions.	
1-06-76	Filed response of deft. Roger S.Berlind to pltff's request for admissions (filed 12-19-75)	
1-19-76	Filed response of deft. S.I.Weill to pltff's request for admissions. (Filed 12-19-75.)	
1-06-75	Filed response of Shearson Hayden Stone to pltff's request for admissions. (Filed 12-19-75)	
1-05-76	Filed response of deft. Bernstein-Macaulay to pltff's request for admissions.(Filed 12-19-75.)	
1-08-76	Filed pltff's memorandum in opposition to motion by Hayden Stone deft's.	
1-08-76	Filed affidavit of J.P.Dailey in opposition to motion by Hayden Stone deft's.	
1-08-76	Filed pltff's memorandum in opposition to deft. Citibank's motion.	
1-08-76	Filed affidavit of J.P.Dailey in opposition to deft.First National Bank Re: production motion.	
1-07-76	Filed affidavit of V.R.Fitzpatrick,Jr.in respect of certain documents.	
1-05-76	Filed interrogs of deft. & cross-claim deft. H.Orenstein.	
1-05-76	Filed interrogs of deff & cross claim deft. H.Orenstein to deft.	
1-06-76	Filed response of Hayden Stone deft's to pltff's supplementary request for admissions.	
1-07-76	Filed deft. First Nat'l City Bank's request for admissions from pltff's.	

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Docket Entries in the Connell action: 72 Civ. 3272

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JUDGE KNAPP

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DATE	PROCEEDINGS
01-07-76	Filed deft's First Nat'l City Bank's request for admissions.
01-07-76	Filed deft's " " " " notice of corrections to be made to pages 2,31 & 77 of deft. Citibank's revised request for admissions from pltff's.
01-07-76	Filed pltff's notice to take deposition of Mahlon M. Frankhauser.
01-06-76	Filed ORDER THAT motion of the Hayden Stone deft's for reargument granting deft. Orenstein's motion for severance & a separate trial is vacated & the motion of deft. Orenstein for severance & separate trial is denied. All counsel are directed to appear before Magistrate Schreiber on 1-12-76 at 11:00 A.M. to complete the appropriate pre-trial orders. Knapp, J.
01-13-76	Filed Deposition of Frank E. Wolf, taken by deft's on 3-12-74.
01-13-76	Filed Deposition of pltff. J. Forzanotaken by deft's on 8-9-74.
01-13-76	Filed " " Saul Solomon taken by deft's on 2-20-75.
01-13-76	Filed " " Pltff, W.A. Hennessey taken by deft's on 1-18-
01-13-76	Filed " of pltff. J. Canario taken by deft's on 2-18-75.
01-13-76	Filed " " " R. Markey by deft. on 8-6-74.
~~01-13-76~~	~~Filed deposition of pltff, Benjamin Young dated 2-19-75, m/n~~
~~01-14-76~~	~~Filed deposition of Rossell B. Newton, Jr. dated 10-3-74, m/n~~
~~01-14-76~~	~~Filed depsotion of Lloyd Smith dated 10-1-74, m/n~~
~~01-14-76~~	~~Filed deposition of Mark Hulsey, Jr. dated 10-2-74, m/n~~
~~01-16-76~~	~~Filed deposition of pltff, Madison Fund, Inc, by Edward A. Merkle dated 3-19-74, m/n~~
~~01-16-76~~	~~Filed deposition (cont'd.) of Madison Fund, Inc, by Edward A. Merkle, dated 4-9-74, m/n~~
01-15-76	Filed revised responses of pltffs. to requests for admissions by the Hayden Stone Defts.
01-16-76	Filed First National City Bank's memorandum of law in response to the request by Magistrate Schreiber for a memorandum.
01-16-76	Filed Hayden Stone Deft's Preliminary trial memorandum.
01-20-76	Filed pltff's U.S. Steel response to deft's First National Bank 2nd revised requests for admissions.
01-12-76	BEFORE SCHREIBER MAGISTRATE PRE-TRIAL CONFERENCE HELD.
01-16-76	Filed deposition of Thomas M. Ramseur, Jr. dated 9-5-75. m/n
01-16-76	" cont'd. " " " " 9-8-75. m/n
01-16-76	Filed deposition of Joseph Hinsey dated 9-9-75. m/n
01-16-76	" cont'd. " " " " 9-25-75. m/n
01-16-76	" " " " " " 10-2-75, m/n
01-22-76	Filed deposition of John C. Provine dated 9-15-75. m/n
01-22-76	" cont'd." " " " 9-17-75. m/n
01-22-76	" " " " " " 9-22-75. m/n
01-22-76	Filed deposition of John J. McNally dated 10-17-75. m/n
01-26-76	Filed trial memorandum of pltff's Lester Connell etal.
01-27-76	Filed Memo-Decision #43782: I am, accordingly, constrained to overrule pltff's objection to the deposition questions at issue. So ordered, Knapp, J. m/n
2-3-76	Filed deposition of U.S. Steel and Carnegie Pension Fund, Inc. by Wm. H. Land dated 2-11-75. m/n
2-3-76	Filed cont'd. depsotion of U.S. Steel and Carnegie Pension Fund, Inc. by Harvey Mole dated9-23-75. m/n
2-3-76	Filed deposition of George F.H. Nelson dated 3-13-75. m/n
2-3-76	Fileddeposition of U.S. Steel by Wilbert A. Walker dated 3-13-75. m/n
2-3-76	Filed deposition of pltff. U.S. Steel and Carnegie Pension Fund, Inc. by Graham O. Harrison dated 2-14-75. m/n

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Docket Entries in the *Connell* *action: 72 Civ. 3272*

Page 9 Judge Knapp U.S. Steel et al. -vs- Harry Oreastein,et al

DATE	PROCEEDINGS
02-03-76	Filedcont'd. deposition of pltff. U.S. Steel and Carnegie Pension Fund Inc. by Henry L. Thompson dated 2-7-75. mn/
02-03-76	Filed deposition of pltff. U.S. Steel and Carnegie Pension Fund,Inc. by W. Bruce Thomas dated 2-12-75. m/n
02-09-76	Filed Document,Deposition & witness lists of deft. & cross-claimant Peter L. Bernstein.
02-09-76	Filed Trial memorandum of deft. & cross-claimant Peter L.Bernstein.
02-09-76	Filed affidavit of service by George Rowe,Jr. of copies of trial memora deposition & witness lists on 2-9-76.
02-11-76	Filed Order that the memo. & order dated 1-26-76 is supplemented in the following respect on page 4, 3 lines from the bottom, add after th word "reasoning", at least to the extent indicated in the next Sentence". So ordered. Knapp,J.
02-17-76	Filed deposition of Richard H. Davimos taken by pltff's on 8-14-74.
02-17-76	Filed deposition of Leonard M. Richards taken by pltff. Lester Connell on 6-11-74.
02-18-76	Filed [illegible] Connell pltff's schedule of exhibits,deposition excerpts & [illegible] to be offered in evidence.
02-10-76	Filed Connell pltff's response to revised requests for admissions of deft Citibank.
02-10-76	Filed Revised response of Connell pltff's to request for admissions of the Hayden-Stone deft's.
02-11-76	Filed deposition of pltff. Frank Scotto taken by deft's on 2-20-75. m/n
02-19-76	Filed deposition of Peter L. Bernstein taken by pltff. on 4-26-73.
02-25-76	Filed Trial memorandum of the Hayden Stone Defts.
02-18-76	Filed stip & order that action is discontinued as to U.S. Steel,Carnegie Pension Fund,Connecticut Mutual Life Ins. National Bank of Commer of Dallas, & Hayden Stone, Bernstein-Macaulay,Roger S. Berlind, & Weill, Henry Orenstein,without prejudice & shall not affect the rights of pltffs against the First National City Bank. Knapp,J.
03-08-76	Filed Memo-Order #44012: On the court's own motion, the record is reopen for the limited purpose of hearing Walter Jeffers as a court's witness. Deft. is directed to produce said witness at a time agreed upon between counsel & chambers,etc. So ordered. Knapp,J.
03-16-76	Filed Supplemental Order that the testimony of Walter Jeffers will be heard in Room 519 on Friday 3-19-76 at 9:30 A.M. On or before noon Thursday, March 18,deft. will deliver to chambers transcript Diary & memorandum etc. Knapp,J.
02-17-76	Before Knapp,J. Non-Jury trial begun.
02-18-76	Trial continued.
02-19-76	" "
02-20-76	" "
02-23-76	" "
02-24-76	" "
02-25-76	" "
03-01-76	" "
03-02-76	" "
03-03-76	" " & concluded. Judge's decision reserved.
03-31-76	Filed pltff's response to request for admissions served by deft. First National City Bank.
4-01-76	Filed transcript of record of proceedings dated 1-23-76.
4-01-76	Filed " " " " " 1-23-76.

Cont'd on page #10

Docket Entries in the Connell action: 72 Civ. 3272

Civ.3272 Lester Connell,etal vs. Bernstein-Macaulay, etal 72 Civ 3272

Page #10

DATE	PROCEEDINGS
05-05-76	Filed stip & order that Lester Connell,etal as Trustees of the Local 816 Labor referred to as the "plaintiffs" & the Hayden Stone deft's is discontinued with prejudice as against the Hayden Stone deft's. This stip is without prejudice to & shall not affect the rights of the pltff's against the First National City Bank("Citi-bank") So ordered. Knapp,J.
04-01-76	Filed transcript of record of proceedings, dated 2/16,18,19,20,23,24/76
04-01-76	Filed transcript of record of proceedings, dated 2/25 & 3/1,2,3/76
08-04-76	Filed Opinion # 44918. Accordingly pltff's. complaints are dismissed. Let deft. submit judgement on five (5) days notice KNAPP J. MN
09-15-76	Filed Supplementary: Opinion #45090: The phrase quoted as indicated will be accordingly be deleted from the opinion. etc. Knapp,J. m/n
09-21-76	Filed Judgment: Ordered that the pltff's herein take nothing that the actions be dismissed with prejudice, on the merits as to deft, Citibank N.A.(formerly known as First National City Bank) & that deft. Citibank,N.A. recover its costs of actionto be taxed from pltff's. Knapp,J. Judgment Ent.Clerk Mailed notice. Ent.9-22-76.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

UNITED STATES STEEL and CARNEGIE PENSION FUND INC., CONNECTICUT MUTUAL LIFE INSURANCE COMPANY and NATIONAL BANK OF COMMERCE OF DALLAS, (AS TRUSTEE OF THE OMEGA-ALPHA, INC. POOL TRUST), Plaintiffs,	COMPLAINT 74 Civ. 391 CBM JURY TRIAL DEMANDED
-against-	
HENRY ORENSTEIN, FIRST NATIONAL CITY BANK, HAYDEN STONE INC., BERNSTEIN-MACAULAY, INC., ROGER S. BERLIND, and SANFORD I. WEILL, Defendants.	

Plaintiffs, United States Steel and Carnegie Pension Fund Inc., Connecticut Mutual Life Insurance Company, and National Bank of Commerce of Dallas (as trustee for the Omega-Alpha, Inc. Pool Trust), by their attorneys, Breed, Abbott & Morgan, aver:

I

The Parties

A. Plaintiffs

1. United States Steel and Carnegie Pension Fund Inc. (the "Pension Fund") is a corporation organized and existing under the laws of the Commonwealth of Pennsylvania, with its principal office at 71 Broadway, New York, New York 10006; the Pension Fund provides pension benefits to more than 175,000 current employees, as well as approximately 70,000 retired employees now on pension, of United States Steel Corporation and its subsidiaries.

2. Connecticut Mutual Life Insurance Company ("Connecticut Mutual") is an insurance corporation organized and existing under the laws of the State of Connecticut, with its principal office at 140 Garden Street, Hartford, Connecticut 06115.

3. National Bank of Commerce of Dallas (the "Dallas Bank") is a national banking association chartered under the laws of the United States, with its principal office at 1525 Elm Street, Dallas, Texas 75221; the Dallas Bank brings this action as trustee for the Omega-Alpha, Inc. Pool Trust (formerly the Okonite Pooled Trust and hereinafter the "Trust"), which provides pension benefits to more than 2,900 employees of Omega-Alpha, Inc. and its subsidiaries.

B. Defendants

4. Defendant Henry Orenstein ("Orenstein") is a resident of the State of New Jersey who founded, is a principal shareholder in, and at all times relevant to this complaint served as President and Chief Executive Officer of Topper Corporation ("Topper"); Topper is a corporation organized in 1966 under the laws of the State of Delaware which was engaged in the business of manufacturing and selling toys until some time prior to May 7, 1973, when it was adjudicated a bankrupt.

5. Defendant First National City Bank ("Citibank") is a national banking association chartered under the laws of the United States, with its principal office at 399 Park Avenue, New York, New York 10022; at all times since November 30, 1950, Citibank has been party to an agreement with the Pension Fund whereby Citibank is obliged, among other things, to provide the Fund with investment advice; at all times relevant to this complaint, Citibank has loaned money to Topper under an agreement with Topper dated October 4, 1966, as amended from time to time (the

"Financing Agreement"), and has acted as agent for three other banks that at various times also advanced monies to Topper under the Financing Agreement.

6. Defendant Hayden Stone Inc. ("Hayden Stone") is a corporation organized and existing under the laws of the State of Delaware and engaged in the brokerage and investment banking business, which before September 29, 1972 was known as CBWL-Hayden Stone Inc., and which maintains its principal office at 767 Fifth Avenue, New York, New York 10022; since 1967 Hayden Stone has acted as managing underwriter of public offerings and arranged for private placements of Topper securities.

7. Defendant Bernstein-Macaulay, Inc. ("Bernstein-Macaulay") is a corporation organized and existing under the laws of the State of Delaware with its principal office at 767 Fifth Avenue, New York, New York 10022; Bernstein-Macaulay is a wholly-owned subsidiary of Hayden Stone and is registered as an investment adviser pursuant to Section 203 of the Investment Advisers Act of 1940, 15 U.S.C. §80b-3 (the "Investment Advisers Act"); at all times relevant to this complaint, Bernstein-Macaulay acted as the principal adviser with regard to investment of the corpus of the Trust.

8. Defendant Roger S. Berlind ("Berlind") is a resident of the State of New York who at all times relevant to this complaint has been the Chief Executive Officer, a director, Chairman of the Executive Committee, and the owner of more than 12% of the common stock of Hayden Stone; a director and member of the Executive Committee of Bernstein-Macaulay; and a director of, as well as a shareholder in, Topper.

9. Defendant Sanford I. Weill ("Weill") is a resident of the State of New York who at all times relevant to this

complaint has been the Chairman of the Board of Directors, a member of the Executive Committee, and the owner of more than 12% of the common stock of Hayden Stone; a director and member of the Executive Committee of Bernstein-Macaulay; and a director of, as well as a shareholder in, Topper.

II

Jurisdiction and Venue

10. This Court has jurisdiction over claims asserted in:

(a) Counts One, Two and Three of this complaint, under Section 27 of the Securities Exchange Act of 1934, as amended, 15 U.S.C. §78aa (the "Exchange Act");

(b) Counts Four, Five and Six under Section 22(a) of the Securities Act of 1933, as amended, 15 U.S.C. §77v(a) (the "Securities Act");

(c) Count Seven, under Section 214 of the Investment Advisers Act, 15 U.S.C. §80b-14; and

(d) Counts Eight, Nine, Ten and Eleven under principles of jurisdiction pendent to federal claims asserted in Counts One through Seven.

11. Venue is proper in this District for claims asserted in this complaint under Section 27 of the Exchange Act, Section 22(a) of the Securities Act and Section 214 of the Investment Advisers Act.

III

The Bases For This Complaint

12. In essence, this complaint arises from the sale on September 28, 1971 of $5,250,000 of Topper 7 1/2% convertible subordinated notes which were not required to be registered pursuant to the Securities Act (the "Private Placement"). Of such notes, $3 million were purchased by the Pension Fund,

$1 million by Connecticut Mutual, and $250,000 by the Dallas Bank. On the next day, the entire proceeds of the Private Placement were turned over to Citibank to reduce Topper's indebtedness under the Financing Agreement. To effectuate the Private Placement, defendants, singly and in concert, directly and indirectly, by means or instrumentalities of interstate commerce including the mails, engaged in various acts, practices and courses of business which operated as a fraud and deceit upon the plaintiffs, and made untrue statements of material facts and omitted to state material facts necessary to make the statements made, in light of the surrounding circumstances, not misleading. Relying upon such untrue and misleading statements, and misled by such deceits, plaintiffs purchased notes of Topper they would not otherwise have bought.

13. Less than 80 days after the Private Placement, Topper announced that its projected $5 million profit for 1971 would instead be a loss of $10 to $15 million. Thus publicly revealed for the first time were Topper's difficulties which, a year and one-half later, ended with its bankruptcy and with notes purchased by plaintiffs now worthless.

A. Background of Orenstein and Topper

14. Since at least the early 1950's, Orenstein and his uncle Marius Orenstein have engaged in the toy business. In their early days, the Orensteins commenced selling through supermarkets pursuant to a program which allowed for return of toys ordered for the Christmas season but not sold. After some years of this program, in 1960 the Orensteins sold their toy business to the Deluxe Reading Corporation, a subsidiary of the Philadelphia and Reading Corporation, and Orenstein thereupon became President of Deluxe Reading.

15. Though Deluxe Reading commenced phasing out Orenstein's supermarket program in favor of marketing through conventional outlets for toys, its financial losses ran high -- amounting to more than $8 million for the first nine months of 1966 alone. In light of such losses, on October 4, 1966, Philadelphia and Reading sold its subsidiary's toy business to Topper, which was owned and controlled by Orenstein, his uncle Marius and a small group of persons known to Orenstein.

B. The Advent of Citibank

16. On the same day, Topper entered into the Financing Agreement. In return for a first security interest in all Topper receivables, inventory, and other assets, Citibank and one other bank thereby agreed to lend up to 80% of the face amount of receivables which they deemed "eligible" plus added sums related to prescribed values for inventory. The Financing Agreement initially ran until January 31, 1968 and thereafter, as a continuing source for working capital, was renewed year to year. However, the Financing Agreement was subject to termination by any party upon notice to each other party, and by Citibank upon the occurrence of specified defaults by Topper. In addition, the Financing Agreement specified that receivables "eligible" as security could at any time be reduced by Citibank to allow for whatever reserves they might deem necessary and proper, and that Topper could dispose of no significant asset, other than in the ordinary course of its business, without the prior written consent of Citibank.

17. Under the Financing Agreement approximately $20 million was advanced to Topper and paid as part of its purchase price for the business of Deluxe Reading.

18. Though Topper commenced operations on October 4, 1966 with an equity capitalization of $3.2 million, it suffered

net losses in excess of $18.7 million during its first four months. Such losses stemmed in part from heavy returns by customers of toys sold on so-called "bill and hold" arrangements.

19. In this light, Citibank insisted, as a condition to continuing to finance Topper for 1967, that Topper broaden its capital base by promptly securing at least $2 million in new equity or long-term subordinated debt. It was to assist in procuring such new capital that Hayden Stone came upon the scene.

C. The Advent of Hayden Stone

20. Hayden Stone did arrange for such new financing as well as five subsequent financings, both private and public, during the period from late 1967 through 1970. As compensation for its services in connection with such financings, Hayden Stone received from Topper approximately $375,000 plus 101,475 shares of Topper common stock. In addition, as a result of participation in two of the private financings, the Hayden Stone Profit Sharing and Savings Plan Trust ended up with 8,000 shares, and Berlind and Weill with 7,800 shares each, of Topper common stock.

21. The upshot of such financings was that, as 1970 neared its end, Topper had paid off a substantial portion of its debt other than loans under the Financing Agreement. And the maturity of the remainder of such debt had been extended through 1971 until early 1972.

22. Equally important, during the month of December 1970 Topper embarked upon a program which involved invoicing to customers approximately $16 million in toys, on credit terms extending from five to eight months, to be sold by such customers during the spring and early summer of 1971 (the "Spring

1971 Program"). This new and unprecedented program, under which at least $14 million of the merchandise invoiced in December was to be reported as sales during 1970, would enable Topper to show income from continuing operations significantly higher than had been reported for 1969.

23. It was against this background that, following consultation with Hayden Stone, Orenstein and other Topper officials met with Citibank in mid-December 1970 to chart Topper's course for 1971. At such time, the desirability of broadening Topper's capital base and of reducing Topper's indebtedness under the Financing Agreement was discussed. The consensus that emerged was that 1971 appeared ripe for a further public offering of Topper common stock, to be followed by a further borrowing from institutional investors on terms more favorable to Topper than those specified in the Financing Agreement.

D. The Public Offering of Topper Common Stock in April 1971

24. True to this plan, on April 29, 1971, 750,000 shares of Topper common stock were offered to the public through underwriters at $10.50 per share. Of these shares, 649,850 were offered by Topper and the remainder by certain shareholders of Topper.

25. At the time of such public offering, Topper announced its plans to borrow additional funds on a long-term basis from institutional investors.

26. Hayden Stone acted as representative of the underwriters in such public offering. Underwriting discounts and commissions aggregated $630,000, the major portion of which was received by Hayden Stone.

27. From this public offering net proceeds to Topper

approximated $6 million. Substantially all of this sum was applied by Topper to reduce its net borrowings under the Financing Agreement.

E. The September 28, 1971 Private Placement

28. Soon after this public offering, Hayden Stone together with Orenstein and Topper proceeded to prepare a Memorandum which Hayden Stone circulated to potential participants in the Private Placement (the "Memorandum"). Received by the Pension Fund and Connecticut Mutual in late July 1971, the Memorandum recited that Hayden Stone would act as Topper's agent for the proposed Private Placement and that the net proceeds would go to reduce Topper's indebtedness under the Financing Agreement. The Memorandum also projected for 1971 net sales of $68 million and a pre-tax income of just under $5.2 million.

29. Inserted in the Memorandum was the Topper Prospectus dated April 29, 1971. Included in the Prospectus, and accorded particular weight by the Pension Fund as well as Connecticut Mutual, were various financial statements of Topper audited by the independent certified public accountants for Topper. Thus, Topper's Consolidated Statement of Operations for 1970 showed after-tax income from continuing operations of $1.5 million -- up some 14% from the comparable figure for 1969 -- and net sales in excess of $63.9 million. With regard to that 1970 net sales figure, a Note to the Consolidated Financial Statement stated simply that approximately $14 million of sales reported by Topper for December 1970 carried extended credit terms of five to eight months and that the comparable amount for the prior December was $2 million.

30. In truth and in fact, this $14 million in sales made up 22% of the sales Topper reported for 1970 and comprised

merchandise invoiced in December 1970 under the Spring 1971 Program. At least half of such merchandise was invoiced subject to the right of customers to return or exchange such wares in 1971 or to "redate" receivables if the merchandise had not been sold when the receivables became due. In addition, much of such merchandise supposedly sold in 1970 was simply stored in public warehouses on the premises of Topper and elsewhere--but at no cost or risk to customers.

31. In light of such rights and of such storage practice, substantial portions of Topper's 1970 purported sales should not have been reported as such. Indeed, after learning of arrangements by Topper with its customers "providing for rights of return, exchange and other concessions applicable to 1970 sales", the independent certified public accountants for Topper, on January 15, 1973, withdrew their certification of Topper's financial statements for 1970. Though such accountants were unable precisely to determine the effect of such rights and concessions on Topper's financial statement for 1970, had Topper's audited financial statements been reported correctly and in accordance with generally accepted accounting principles, Topper's Consolidated Statement of Operations would have shown significant losses--rather than a profit from continuing operations--for 1970.

32. Misrepresenting this true state of affairs, the Memorandum referred to the $14 million in "sales" reported for December 1970 under the Spring 1971 Program, but never mentioned such provisions for return or exchange of merchandise in 1971 or for the "redating" of receivables. Indeed, just contrary to the true facts, the Memorandum represented that merchandise invoiced in 1970 under the Spring 1971 Program had enjoyed an excellent reception during the first quarter of 1971

and appeared to be selling on a year-round basis, thus serving to reduce seasonal fluctuations in Topper's sales and earnings.

33. Following receipt of the Memorandum, the Pension Fund made inquiry of a director of Topper otherwise known to the Fund. That director referred to Topper's prior practice of selling on consignment, with provisions for return of merchandise unsold after the Christmas season, and stated that such practice had been abandoned.

34. As a next step, at meetings in August of 1971 with officials of Hayden Stone and Topper, including Orenstein, both Connecticut Mutual and the Pension Fund received assurances as to the worth of Topper's receivables and Topper's procedures for checking on sales of its products. Thus Topper advised the Fund that at that time of the year Topper maintained day-to-day checks on movements from warehouses to customers and from customers' shelves; similarly, in the presence of Hayden Stone, Topper represented to Connecticut Mutual that receivables from its $14 million in reported sales during December 1970 were being paid off as due; further, given to both Connecticut Mutual and to the Pension Fund by Topper were materials representing that Topper monitored the "aging" of its accounts receivable by computer so that aging reports were prepared quickly after the end of the month, both in summary and detail form by account.

35. By way of final assurance, Topper referred to the substantial sums advanced by banks to Topper and to Citibank's role in policing daily cash receipts and receivables of Topper under the Financing Agreement. Both Connecticut Mutual and the Pension Fund were advised that each should feel free to check with lenders to Topper, particularly with Citibank.

36. As agent for each bank acting as a participant or

sub-participant under the Financing Agreement, Citibank functioned as if it "were the sole lender hereunder". Citibank was thus charged with responsibility for making all advances, receiving all assignments of receivables and all collections, and dealing with collateral and security interests. In this capacity, hand delivered to Citibank practically each working day by Topper were all collections from each of its customers as well as merchandise return reports listing each return received from each customer on each receivable previously assigned to Citibank. In addition, following the end of each month, typically by no more than 5 to 7 days into the next month, Topper delivered to Citibank an accounts receivable detail trial balance, as adjusted by hand, plus a summary of that detail trial balance by account, and some few weeks later, unaudited financial statements.

37. Accepting Topper's invitation to check with Citibank, on or about August 25, 1971, the Pension Fund telephoned Walter Jeffers, the Vice-President of Citibank responsible for the Pension Fund's account, including coordinating the rendering of "investment advice" pursuant to the Fund's aforementioned agreement with Citibank. By that telephone conversation Mr. Jeffers was advised that the Pension Fund was considering an investment in Topper and asked for whatever information was in the possession of Citibank that might bear on such decision.

38. In apparent response, on August 27, 1971, Mr. Edward Waldman of Citibank telephoned the Fund. In the course of that telephone conversation, Mr. Waldman was asked, among other things:

(a) the size of Citibank's loan participation, to which he replied, "several million dollars";

(b) why the interest rate was so high under the Financing Agreement, to which he responded that one of the reasons was that the bank performed audits of Topper's receivables;

(c) whether Topper had shown itself to be competent in these audits and had good internal accounting controls, to which he replied, "yes";

(d) if he knew of any current problem in Topper, to which he replied, "no";

(e) whether Mr. Waldman anticipated any problems in Topper, to which he again replied, "no".

39. Just contrary to Citibank's assurances that there were no current problems in Topper and that none were anticipated, materials from Topper then in the possession of Citibank revealed that during the 31-day period from June 30 to July 31, 1971:

(a) receivables more than 60 days past due had increased from $1.2 million to $7.2 million and, as a percentage of all accounts receivable, from 3.8% as of June 30 to 21.4% by July 31, 1971;

(b) receivables deemed "ineligible" as security under the Financing Agreement (i.e., not paid within 60 days following the end of the month in which they became due or otherwise deemed by the banks inadequate for security) increased from $8.6 million to $13.6 million and, as a percentage of all accounts receivable, from 25.7% as of June 30 to 40.3% by July 31, 1971; this $5 million increase in "ineligible" receivables represented more than one-half of the $9.5 million of merchandise invoiced on 5-month extended credit terms in December 1970, under the Spring 1971 Program, on which payment was due during May of 1971, and which therefore became "ineligible" unless paid off on or before July 31, 1971; and

(c) because such receivables had gone sour, receipts of Topper delivered to Citibank during the month of July 1971 fell 40% short of receipts as previously projected by Topper to Citibank.

40. Indeed, assurances by Citibank to the Pension Fund ran counter to actions by Citibank itself, actions taken just before the time such assurances were made. Thus, on July 15, 1971, the Financing Agreement was amended by Citibank to increase Topper's borrowing limit until August 15 from $20 to $21 million, and to allow for advances up to $3 million in excess of the Agreement's ceiling of 80% of "eligible" receivables. Again, on August 25, 1971, two days before the assurances by Citibank to the Pension Fund, Citibank extended the period during which the $21 million loan ceiling might endure from August 15 to September 30, 1971 -- just long enough to tide Topper over the Private Placement on September 28th; and at the same time Citibank increased from $3 million to $4.8 million the Financing Agreement's limit on permissible borrowings in excess of 80% of "eligible" receivables.

41. With the Pension Fund thus falsely comforted, Hayden Stone informed Connecticut Mutual that the Pension Fund was contemplating the purchase of a major portion of the notes. In light of such assurance and other representations made in the course of its prior investigation, Connecticut Mutual thereupon committed to purchase $1 million of the notes.

42. On or about September 17, 1971, the Chairman of the Executive Committee of Bernstein-Macaulay telephoned the Dallas Bank to recommend the participation by the Trust in the forthcoming Private Placement. Representing that "we" have for some time acted as Topper's investment banker and consequently well know Topper's affairs, he stated that Topper's

stock then selling at approximately $12 a share would be worth $40 per share within two years. Soon after this telephone call, the Dallas Bank received the Memorandum through the mails from Bernstein-Macaulay. After learning from Bernstein-Macaulay that the Pension Fund and Connecticut Mutual planned to purchase the major portion of the proposed Private Placement, the Dallas Bank acted on the recommendation of Bernstein-Macaulay and committed to invest $250,000 for the benefit of the Trust.

43. Unbeknownst to the Dallas Bank, however, the Chairman of the Executive Committee of Bernstein-Macaulay made this recommendation only at the insistence of Hayden Stone and despite the fact that such advice, as he admitted to the Dallas Bank some months after the Private Placement, ran counter to the best judgment of Bernstein-Macaulay at the time.

44. As September of 1971 wore on, materials that came into the possession of Citibank reflected even further deterioration in the finances of Topper. Thus, summary data prepared by Topper and delivered to Citibank under the Financing Agreement on or before September 10, 1971, showed that an additional $500,000 of Topper receivables had become "ineligible" during August. Moreover, data delivered by Topper to Citibank on a daily basis showed that major Topper customers continued to withhold funds reportedly due under the Spring 1971 Program. The upshot was that by September's end "ineligible" receivables had jumped another $3 million to a total of $17.2 million, and Topper's cash flow for September continued to fall far short of its projections as it had for August.

45. Just prior to the Private Placement, Citibank, Berlind and Weill received from Topper unaudited Consolidated Financial Statements for the seven-month period ending July 31, 1971. These showed that for the month of July Topper had

suffered a net loss before federal income taxes in excess of $360,000. Though the Pension Fund and Connecticut Mutual had been shown such unaudited financials for the six-month period ending June 30, 1971, not disclosed prior to the Private Placement were comparable figures for July. Losses for that one month of July, however, had wiped out roughly 60 percent of Topper's net income before federal income taxes for the first six months of 1971, as previously reported in the financials that were shown to the Pension Fund and Connecticut Mutual.

46. Despite the facts alleged in Paragraphs 30, 31, 39, 40, 44 and 45 above, the Private Placement Purchase Agreement, dated September 28, 1971 referred to Topper's audited financial statements as of December 31, 1970; referred to various unaudited financial statements as of June 30, 1971 which showed, among other things, a pre-tax income of some $600,000 for the first six months of 1971; and thereafter included a representation by Topper that, since that latter date, there had been no materially adverse change in the business or condition (financial or otherwise) of Topper.

47. In the negotiation of said Purchase Agreement Hayden Stone participated on behalf of Topper.

48. Prior to September 28, 1971 said Purchase Agreement was reviewed, and at least key provisions thereof approved, by Citibank.

49. On September 28, 1971, pursuant to said Purchase Agreement and relying upon the representations therein, as well as other representations of material facts theretofore made, the Pension Fund purchased $3 million, Connecticut Mutual purchased $1 million, and the Dallas Bank purchased $250,000 of notes from Topper.

50. The next day the entire proceeds of the Private

Placement were turned over to Citibank in reduction of Topper's indebtedness under the Financing Agreement.

51. Hayden Stone was paid some $207,500 by Topper for its services in connection with the Private Placement.

52. However, just 60 days or so following the Private Placement, on December 2, 1971, Topper announced that its sales and earnings for 1971 "will be quite disappointing." Two weeks later, on December 17, Topper revealed that, instead of enjoying a more than $5 million profit as projected a short time before, it would suffer 1971 losses of as much as $10 million to $15 million as a result of being forced to accept merchandise for exchange or return.

53. Topper never recovered from the failure of its Spring 1971 Program, as compounded by the continuation of the same terms and conditions for merchandise invoiced by Topper during early and mid-1971. The great bulk of merchandise thus invoiced was either never shipped from the Topper warehouse or was returned by Topper customers. And on May 7, 1973 Topper was adjudicated a bankrupt.

54. Facts alleged in Paragraphs 30, 31, 39, 40, 43, 44 and 45 above were known or should have been known to Topper, Orenstein, Citibank, Hayden Stone, Bernstein-Macaulay, Berlind, and Weill prior to September 28, 1971, but at no time prior to the Private Placement were such facts revealed to the Pension Fund, Connecticut Mutual, or the Dallas Bank.

55. In fact, just to the contrary, Hayden Stone represented in its Memorandum that merchandise invoiced under the Spring 1971 Program had enjoyed an excellent reception; Topper represented that its receivables resulting from the Spring 1971 Program were being paid off as they became due; Citibank represented to the Pension Fund that there were no

current problems in Topper and that none were anticipated; Topper represented that, as of September 28, 1971, there had been no recent materially adverse change in its business; Hayden Stone recommended participation in the Private Placement to the Pension Fund and Connecticut Mutual; and Hayden Stone, Berlind and Weill caused Bernstein-Macaulay to make the same recommendation to the Dallas Bank.

56. While such recommendations by Hayden Stone were outstanding, the Hayden Stone Profit Sharing and Savings Plan Trust itself sold 8,000 shares of Topper common stock, on August 19, 1971, at a price of $14.50 per share. These shares comprised all Topper common stock held by such profit sharing trust, Hayden Stone, Berlind, or Weill which had been registered for public sale. In addition, Berlind and Weill, whose ownership of Topper common stock had been represented to the Pension Fund by Hayden Stone as their largest personal holding, requested from Topper, either before or shortly after the Private Placement, a Registration Statement to enable their public offering of such stock. Neither the fact of such sale nor of such intention to sell was disclosed to the Pension Fund, Connecticut Mutual, or the Dallas Bank prior to September 28, 1971.

57. The Pension Fund, Connecticut Mutual and the Dallas Bank first learned of the facts alleged in Paragraphs 30, 31, 39, 40, 44, 45 and 56 above during 1973, in the course of their investigations that preceded the filing of this complaint.

IV. COUNT ONE

Violations of Section 10(b) of the Exchange Act and Rule 10b-5 Promulgated Thereunder

58. The Pension Fund, Connecticut Mutual, and the Dallas Bank are plaintiffs in this count against all defendants.

59. Plaintiffs reaver Paragraphs 1 through 57 of

this complaint.

60. By reason of the averments incorporated in Paragraph 59 of this complaint, singly and in concert, directly and indirectly: Topper, Orenstein, Hayden Stone, Bernstein-Macaulay, Berlind, Weill, and Citibank have violated Section 10(b) of the Exchange Act and Rule 10b-5, 17 C.F.R. §240.10b-5, promulgated thereunder; Hayden Stone, Bernstein-Macaulay, Berlind, Weill and Citibank aided and abetted Topper and Orenstein in said violations; Hayden Stone, Berlind and Weill aided and abetted Bernstein-Macaulay in said violations; and as a consequence, plaintiffs have been damaged.

V. COUNT TWO

Violation of Section 15(c)(1) of the Exchange Act and Rule 15c1-2 Thereunder

61. The Pension Fund, Connecticut Mutual, and the Dallas Bank are plaintiffs in this count against Hayden Stone.

62. Plaintiffs reaver Paragraph 59 of this complaint.

63. By reason of the averments incorporated in Paragraph 62 of this complaint, defendant Hayden Stone has violated Section 15(c)(1) of the Exchange Act and Rule 15c1-2, 17 C.F.R. §240.15c1-2, promulgated thereunder and, as a consequence, plaintiffs have been damaged.

VI. COUNT THREE

Violation of Section 20(a) of the Exchange Act

64. The Pension Fund, Connecticut Mutual, and the Dallas Bank are plaintiffs in this count against Orenstein, Citibank, Hayden Stone, Berlind, and Weill.

65. Plaintiffs reaver Paragraphs 59, 60 and 63 of this complaint.

66. By reason of the averments incorporated in Paragraph 65 of this complaint: Orenstein and Citibank controlled

Topper; Berlind and Weill controlled Hayden Stone; and Hayden Stone, Berlind, and Weill controlled Bernstein-Macaulay; each within the meaning of Section 20 of the Exchange Act, and therefore are jointly and severally liable to plaintiffs for the aforementioned violations of Sections 10(b) and 15(c)(1) of the Exchange Act.

VII. COUNT FOUR

Violations of Section 12(2) of the Securities Act

67. The Pension Fund, Connecticut Mutual, and the Dallas Bank are plaintiffs in this count against Orenstein, Hayden Stone, Bernstein-Macaulay, Berlind, Weill, and Citibank.

68. Plaintiffs reaver Paragraph 59 of this complaint.

69. By reason of the averments incorporated in Paragraph 68 of this complaint, singly and in concert, directly and indirectly: Topper, Orenstein, Hayden Stone and Bernstein-Macaulay have violated Section 12(2) of the Securities Act; Hayden Stone, Bernstein-Macaulay and Citibank aided and abetted Topper and Orenstein in said violations; Hayden Stone, Berlind and Weill aided and abetted Bernstein-Macaulay in said violations; and, as a consequence, plaintiffs have been damaged.

VIII. COUNT FIVE

Violations of Section 17(a) of the Securities Act

70. The Pension Fund, Connecticut Mutual, and the Dallas Bank are plaintiffs in this count against Orenstein, Citibank, Hayden Stone, Bernstein-Macaulay, Berlind, and Weill.

71. Plaintiffs reaver Paragraph 59 of this complaint.

72. By reason of the averments incorporated in

Paragraph 71 of this complaint, singly and in concert, directly and indirectly: Topper, Orenstein, Hayden Stone and Bernstein-Macaulay have violated Section 17(a) of the Securities Act; Hayden Stone, Bernstein-Macaulay and Citibank aided and abetted Topper and Orenstein in said violation; Hayden Stone, Berlind and Weill aided and abetted Bernstein-Macaulay in said violations; and, as a consequence, plaintiffs have been damaged.

IX. COUNT SIX

Violations of Section 15 of the Securities Act

73. The Pension Fund, Connecticut Mutual, and the Dallas Bank are plaintiffs in this count against Orenstein, Citibank, Hayden Stone, Berlind, and Weill.

74. Plaintiffs reaver Paragraphs 59 and 69 of this complaint.

75. By reason of the averments in Paragraph 74 of this complaint: Orenstein and Citibank controlled Topper; Berlind and Weill controlled Hayden Stone; and Hayden Stone, Berlind and Weill controlled Bernstein-Macaulay; each within the meaning of Section 15 of the Securities Act, and therefore are jointly and severally liable to plaintiffs for the aforementioned violations of Section 12(2) of the Securities Act.

X. COUNT SEVEN

Violation of Section 206(2) of The Investment Advisers Act

76. The Dallas Bank is plaintiff in this count against Bernstein-Macaulay.

77. Plaintiff reavers Paragraph 59 of this complaint.

78. By reason of the averments incorporated in Paragraph 77 of this complaint, Bernstein-Macaulay violated Section 206(2) of the Investment Advisers Act and, as a consequence,

plaintiff has been damaged.

XI. COUNT EIGHT

Unjust Enrichment Under Common Law

79. The Pension Fund, Connecticut Mutual, and the Dallas Bank are plaintiffs in this count against Citibank.

80. Plaintiffs reaver the averments incorporated in Paragraph 59 of this complaint.

81. By reason of the averments incorporated in Paragraph 80 of this complaint, defendant Citibank has been unjustly enriched at the expense of plaintiffs in the amount of $4,250,000.

XII. COUNT NINE

Common Law Fraud and Deceit by Defendants Orenstein and Citibank and by Topper

82. The Pension Fund and Connecticut Mutual are plaintiffs in this count against Orenstein and Citibank.

83. Plaintiff reavers Paragraph 59 of this complaint.

84. By reason of the allegations incorporated in Paragraph 83 of this complaint, Topper, Orenstein, and Citibank, directly and indirectly, singly and in concert, have committed acts constituting fraud and deceit upon the Pension Fund and upon Connecticut Mutual by making material misrepresentations which they knew or should have known to be false, and on which the Pension Fund and Connecticut Mutual justifiably relied to their detriment, in order to induce the Pension Fund and Connecticut Mutual to participate in the Private Placement.

XIII. COUNT TEN

Common Law Fraud and Deceit by Defendant Bernstein-Macaulay

85. The Dallas Bank is plaintiff in this count against Dernstein-Macaulay.

86. Plaintiff reavers the averments incorporated in Paragraph 59 of this complaint.

87. By reason of the averments incorporated in Paragraph 86 of this complaint, Bernstein-Macaulay has committed acts constituting fraud and deceit upon the Dallas Bank by making material misrepresentations which it knew or should have known to be false, and on which the Dallas Bank justifiably relied to its detriment, in order to induce the Dallas Bank to participate in the Private Placement.

XIV. COUNT ELEVEN

Common Law Breach Of Fiduciary Duty

88. The Pension Fund is plaintiff in this count against Citibank.

89. Plaintiff reavers the averments incorporated in Paragraph 59 of this complaint.

90. By reason of the averments incorporated in Paragraph 89 of this complaint, Citibank breached fiduciary duties owed to the Pension Fund at common law.

PRAYER FOR RELIEF

WHEREFORE, plaintiffs pray for judgment against defendants as follows:

AS TO COUNT ONE

91. Against all defendants and in favor of all plaintiffs in the amount of $4,250,000, together with interest, costs, disbursements and such other relief as the Court may deem just and proper.

AS TO COUNT TWO

92. Against defendant Hayden Stone and in favor of all plaintiffs in the amount of $4,250,000, together with interest, costs, disbursements and such other relief as the Court may deem just and proper.

AS TO COUNT THREE

93. Against defendants Orenstein, Citibank, Hayden

Stone, Berlind, and Weill and in favor of all plaintiffs in the amount of $4,250,000, together with interest, costs, disbursements and such other relief as the Court may deem just and proper.

AS TO COUNTS FOUR AND FIVE

94. Against defendants Orenstein, Citibank, Hayden Stone, Bernstein-Macaulay, Berlind, and Weill and in favor of all plaintiffs in the amount of $4,250,000, together with interest, costs, disbursements, attorney's fees, and such other relief as the Court may deem just and proper.

AS TO COUNT SIX

95. Against defendants Orenstein, Citibank, Hayden Stone, Berlind, and Weill and in favor of all plaintiffs in the amount of $4,250,000, together with interest, costs, disbursements, attorney's fees, and such other relief as the Court may deem just and proper.

AS TO COUNT SEVEN

96. Against defendant Bernstein-Macaulay and in sole favor of the Dallas Bank in the amount of $250,000, together with interest, costs, disbursements and such other relief as the Court may deem just and proper.

AS TO COUNT EIGHT

97. Against defendant Citibank and in favor of all plaintiffs in the amount of $4,250,000 as compensatory damages, and against defendant Citibank in the amount of $1,000,000 as exemplary damages, together with interest, costs, disbursements, and such other relief as the Court may deem just and proper.

AS TO COUNT NINE

98. Against defendants Orenstein and Citibank and in favor of the Pension Fund and Connecticut Mutual in the amount of $4 million as compensatory damages, and against defendant

Citibank in the amount of $1 million as exemplary damages, together with interest, costs, disbursements, and such other relief as the Court may deem just and proper.

AS TO COUNT TEN

99. Against defendant Bernstein-Macaulay and in sole favor of the Dallas Bank in the amount of $250,000 as compensatory damages, and in the amount of $100,000 as exemplary damages, together with interest, costs, disbursements, and such other relief as the Court may deem just and proper.

AS TO COUNT ELEVEN

100. Against defendant Citibank and in sole favor of the Pension Fund in the amount of $3 million as compensatory damages, and in the amount of $1 million as exemplary damages, together with interest, costs, disbursements, and such other relief as the Court may deem just and proper.

Dated: January 23, 1974

BREED, ABBOTT & MORGAN

By Robert A Bicks

Attorneys for Plaintiffs
1 Chase Manhattan Plaza
New York, New York 10005
(212) 944-4800

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

COPY RECEIVED BY
MAR 29 1974
BREED, ABBOTT & MORGAN
ATTY'S FOR: CBM

---------------------------------------x

UNITED STATES STEEL AND
CARNEGIE PENSION FUND, INC., et al.,

Plaintiffs,

-against-

HENRY ORENSTEIN, et al.,

Defendants.

---------------------------------------x

ANSWER

First National City Bank ("Citibank"), by its attorneys, Shearman and Sterling, answers the complaint herein as follows:

1. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 1 of the complaint, except admits, on information and belief, that United States Steel and Carnegie Pension Fund, Inc. ("Pension Fund") is a corporation and that Pension Fund has an office in New York, New York.

2. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 2 of the complaint, except admits, on information and belief, that Connecticut Mutual Life Insurance Company ("Connecticut Mutual") is a corporation.

3. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 3 of the complaint, except admits, on information and belief, that the National Bank of Commerce of Dallas ("Dallas Bank") is a national banking association.

4. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 4 of the complaint, except admits, on

information and belief, that Henry Orenstein ("Orenstein") served as President and Chief Executive Officer of Topper Corporation ("Topper"), that Topper is a corporation which was engaged in the business of manufacturing and selling toys and that on or about May 7, 1973, Topper was adjudicated a bankrupt.

5. Denies each and every allegation contained in paragraph 5 of the complaint, except admits that Citibank is a national banking association chartered under the laws of the United States, with its principal office at 399 Park Avenue, New York, New York 10022, that Citibank entered into an agreement with Pension Fund, dated November 30, 1950, reference to which is made for the terms thereof, that Citibank entered into an agreement with Manufacturers Hanover Trust Company ("Manufacturers") and DeLuxe Topper Corporation, a predecessor corporation to Topper, dated October 4, 1966, which agreement has been amended from time to time ("Financing Agreement"), reference to which is made for the terms thereof, and that Citibank has acted as agent for Manufacturers and Ford Motor Credit Corporation, which, together with Citibank, from time to time advanced monies to Topper.

6. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 6 of the complaint, except admits, on information and belief, that Hayden Stone Inc. ("Hayden Stone") is a corporation engaged in the brokerage and investment banking business, which at one time was known as CBWL-Hayden, Stone Inc., and that Hayden Stone maintains an office in New York, New York.

7. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 7 of the complaint.

8. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 8 of the complaint.

9. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 9 of the complaint.

10. Denies each and every allegation contained in paragraph 10 of the complaint, except denies knowledge or information sufficient to form a belief as to the truth of such allegations insofar as they relate to defendants other than Citibank.

11. Admits the allegations contained in paragraph 11 of the complaint.

12. Denies each and every allegation contained in paragraph 12 of the complaint, except denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in the first two sentences of such paragraph, and admits that, on or about September 29, 1971, the sum of $5,250,000 was received by Citibank and was credited to Topper's account in reduction of Topper's indebtedness under the Financing Agreement, which had been $19,752,000.

13. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 13 of the complaint, except admits, on information and belief, that on or about December 17, 1971, Topper announced that its projected $5 million profit for 1971 would instead be a loss of $10 million to $15 million.

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14. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 14 of the complaint.

15. Admits, on information and belief, the allegations contained in paragraph 15 of the complaint.

16. Denies each and every allegation contained in paragraph 16 of the complaint, except admits that on October 4, 1966, Citibank and Topper entered into the Financing Agreement, reference to which is made for the terms thereof, and that the Financing Agreement initially ran until January 31, 1968, and thereafter was renewed from time to time.

17. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 17 of the complaint, except admits that approximately $20 million was advanced to Topper under the Financing Agreement.

18. Denies each and every allegation contained in paragraph 18 of the complaint except admits, on information and belief, the allegations contained in the first sentence of such paragraph and that such losses resulted in part from returns by customers of toys.

19. Denies each and every allegation contained in paragraph 19 of the complaint, except denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in the second sentence of said paragraph.

20. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 20 of the complaint, except admits, on information and belief, that Hayden, Stone arranged certain financings for Topper from late 1967 through 1970.

21. Denies knowledge or information sufficient to form a belief as to the truth of the allegations con-

tained in paragraph 21 of the complaint.

22. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 22 of the complaint.

23. Denies each and every allegation contained in paragraph 23 of the complaint, except admits that representatives of Citibank met with representatives of Topper in December, 1970.

24. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 24 of the complaint, except admits, on information and belief, that on or about April 29, 1971, 750,000 shares of Topper common stock were offered to the public through underwriters at $10.50 per share and that, of these shares, 658,525 were offered by Topper and the remainder by certain shareholders of Topper.

25. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 25 of the complaint.

26. Admits, on information and belief, the allegations contained in paragraph 26 of the complaint.

27. Denies each and every allegation contained in paragraph 27 of the complaint, except admits, on information and belief, that Topper's net proceeds from the public offering were $6,361,351.50 and that, on or about May 7, 1971, $6,361,351.50 was received by Citibank and was credited to Topper's account in reduction of Topper's indebtedness under the Financing Agreement, which had been $15,729,267.50.

28. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 28 of the complaint.

29. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 29 of the complaint.

30. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 30 of the complaint.

31. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 31 of the complaint.

32. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 32 of the complaint.

33. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 33 of the complaint.

34. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 34 of the complaint.

35. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 35 of the complaint.

36. Denies each and every allegation contained in paragraph 36 of the complaint, except, with respect to the first two sentences of said paragraph, makes reference

to the Financing Agreement for the terms thereof, and admits that from time to time there were delivered to Citibank by Topper collections from Topper's customers, merchandise return reports, accounts receivable detail trial balances, certain of which trial balances were as adjusted by hand, summaries of detail trial balances by accounts and unaudited financial statements.

37. Denies each and every allegation contained in paragraph 37 of the complaint, except denies knowledge or information sufficient to form a belief as to the truth of the allegations relating to any invitation by Topper to Pension Fund to check with Citibank, and admits that on or about August 25, 1971 Walter Jeffers, Vice President of Citibank, who was responsible for Pension Fund's account with Citibank pursuant to an agreement between Pension Fund and Citibank, reference to which is made for the terms thereof, received a telephone call from a person identifying himself as a representative of Pension Fund, and that said person requested information concerning Topper.

38. Denies each and every allegation contained in paragraph 38 of the complaint, except admits that on or about August 27, 1971 Mr. Edward Waldman ("Waldman"), Vice President of Citibank, spoke with Henry Thompson ("Thompson") who, upon information and belief, was employed by Pension Fund, and that Waldman told Thompson, among other things, the approximate amount of the Topper loan balance, which was several million dollars.

39. Denies each and every allegation contained in paragraph 39 of the complaint.

40. Denies each and every allegation contained in paragraph 40 of the complaint, except admits that on or about July 20, 1971, Citibank and Topper entered into an amendment to the Financing Agreement, reference to which amendment is made for the terms thereof, and that on or about August 25, 1971 Citibank extended the period for the $21 million loan ceiling from August 15 to September 30, 1971 and increased from $3 million to $4.8 million the Financing Agreement's limit on permissible borrowings in excess of 80% of eligible receivables.

41. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 41 of the complaint.

42. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 42 of the complaint.

43. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 43 of the complaint.

44. Denies each and every allegation contained in paragraph 44 of the complaint.

45. Denies each and every allegation contained in paragraph 45 of the complaint, except denies

knowledge or information sufficient to form a belief as to the truth of the allegations contained in the last two sentences of said paragraph, and admits that Citibank received from Topper unaudited consolidated financial statements for the seven-month period ending July 31, 1971, showing a net loss before taxes in excess of $360,000.

46. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 46 of the complaint.

47. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 47 of the complaint.

48. Denies each and every allegation contained in paragraph 48 of the complaint.

49. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 49 of the complaint.

50. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 50 of the complaint, except admits that on or about September 29, 1971, $5,250,000 was received by Citibank and was credited to Topper's account in reduction of Topper's indebtedness, which had been $19,752,000.

51. Denies knowledge or information sufficent to form a belief as to the truth of the allegations contained in paragraph 51 of the complaint.

52. Admits, on information and belief, the allegations contained in paragraph 52 of the complaint.

53. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 53 of the complaint, except admits, on information and belief, that on or about May 7, 1973, Topper was adjudicated a bankrupt.

54. Denies each and every allegation contained in paragraph 54 of the complaint, except denies knowledge or information sufficient to form a belief as to the truth of such allegations as they relate to plaintiffs or to defendants other than Citibank, and makes reference to Citibank's responses to the allegations contained in paragraphs 30, 31, 39, 40, 43, 44 and 45 of the complaint.

55. Denies each and every allegation contained in paragraph 55 of the complaint, except denies knowledge or information sufficient to form a belief as to the truth of such allegations insofar as they relate to defendants other than Citibank.

56. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 56 of the complaint.

57. Denies knowledge or information sufficient to form a belief as to the truth of the allegations contained in paragraph 57 of the complaint.

58. Admits the allegations contained in paragraph 58 of the complaint.

59. In response to paragraph 59 of the complaint, realleges paragraphs 1 through 57 hereof.

60. Denies each and every allegation contained in paragraph 60 of the complaint, except denies knowledge or information sufficient to form a belief as to the truth of such allegations insofar as they relate to defendants other than Citibank.

61-63. In response to paragraphs 61 through 63 of the complaint, states that no response by Citibank is required.

64. Admits the allegations contained in paragraph 64 of the complaint.

65. In response to paragraph 65 of the complaint, realleges paragraphs 59, 60 and 63 hereof.

66. Denies each and every allegation contained in paragraph 66 of the complaint, except denies knowledge or information sufficient to form a belief as to the truth of such allegations insofar as they relate to defendants other than Citibank.

67. Admits the allegations contained in paragraph 67 of the complaint.

68. In response to paragraph 68 of the complaint, realleges paragraph 59 hereof.

69. Denies each and every allegation contained in paragraph 69 of the complaint, except denies knowledge or information sufficient to form a belief as to the truth of such allegations insofar as they relate to defendants other than Citibank.

70. Admits the allegations contained in paragraph 70 of the complaint.

71. In response to paragraph 71 of the complaint, realleges paragraph 59 hereof.

72. Denies each and every allegation contained in paragraph 72 of the complaint, except denies knowledge or information sufficient to form a belief as to the truth of such allegations insofar as they relate to defendants other than Citibank.

73. Admits the allegations contained in paragraph 73 of the complaint.

74. In response to paragraph 74 of the complaint, realleges paragraphs 59 and 69 herein.

75. Denies each and every allegation contained in paragraph 75 of the complaint, except denies knowledge or information sufficient to form a belief as to the truth of such allegations insofar as they relate to defendants other than Citibank.

76-78. In response to paragraphs 76 through 78 of the complaint, states that no response by Citibank is required.

79. Admits the allegations contained in paragraph 79 of the complaint.

80. In response to paragraph 80 of the complaint, realleges paragraph 59 herein.

81. Denies each and every allegation contained in paragraph 81 of the complaint.

82. Admits the allegations contained in paragraph 82.

83. In response to paragraph 83 of the complaint, realleges paragraph 59 herein.

84. Denies each and every allegation contained in paragraph 84 of the complaint, except denies knowledge or information sufficient to form a belief as to the truth of such allegations insofar as they relate to defendants other than Citibank.

85-87. In response to paragraphs 85 through 87 of the complaint, states that no response by Citibank is required.

88. Admits the allegations contained in paragraph 88 of the complaint.

89. In response to paragraph 89 of the complaint, realleges paragraph 59 herein.

90. Denies each and every allegation contained in paragraph 90 of the complaint.

AS AND FOR A FIRST AFFIRMATIVE
DEFENSE, DEFENDANT CITIBANK
ALLEGES THAT:

91. Whatever damages, if any, were sustained by plaintiffs as a result of the allegations asserted in the complaint, were caused in whole or in part or were contributed to by reason of the carelessness, negligence, or imprudent business judgment of plaintiffs, their officers and directors and their agents.

AS AND FOR A SECOND AFFIRMATIVE
DEFENSE, DEFENDANT CITIBANK
ALLEGES THAT:

92. Plaintiffs may not assert the claims alleged in the complaint, because they, their officers and directors and their agents knew or in the exercise of reasonable diligence should have known of any facts which they claim were misrepresented or not stated to them by Citibank.

AS AND FOR A THIRD AFFIRMATIVE
DEFENSE, DEFENDANT CITIBANK
ALLEGES THAT:

93. The complaint fails to state a claim upon which relief can be granted against Citibank because it does not allege any facts indicating that Citibank owed any duty, contractual, fiduciary or otherwise, to any of plaintiffs with respect to any claims alleged.

AS AND FOR A FOURTH AFFIRMATIVE
DEFENSE, DEFENDANT CITIBANK
ALLEGES THAT:

94. Plaintiffs have failed to state a claim upon which relief can be granted against Citibank based

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on any alleged misrepresentation or omission on the part of Citibank because they do not, and cannot, allege reliance thereon by any plaintiff in taking any action.

AS AND FOR A FIFTH AFFIRMATIVE
DEFENSE, DEFENDANT CITIBANK
ALLEGES THAT:

95. Citibank had no duty to participate in, approve or otherwise review, and did not in fact participate in, approve or otherwise review, Topper's prospectus, Memorandum or Private Placement Purchase Agreement.

AS AND FOR A SIXTH AFFIRMATIVE
DEFENSE, DEFENDANT CITIBANK
ALLEGES THAT:

96. The complaint fails to state a claim upon which relief can be granted against Citibank because it does not allege that Citibank used the United States mail or any means or instrumentality of interstate commerce, directly or indirectly, in connection with any of the violations alleged in the complaint.

AS AND FOR A SEVENTH AFFIRMATIVE
DEFENSE, DEFENDANT CITIBANK
ALLEGES THAT:

97. Count One of the complaint fails to state a claim upon which relief can be granted against Citibank because Citibank acted at all times in good faith and without actual knowledge of any violation of Section 10(b) of the Securities and Exchange Act of 1934, or Rule 10b-5 promulgated thereunder, by Orenstein or Topper, and Citibank did not directly or indirectly induce any such violation.

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AS AND FOR AN EIGHTH AFFIRMATIVE
DEFENSE, DEFENDANT CITIBANK
ALLEGES THAT:

98. Count Four of the complaint fails to state a claim upon which relief can be granted against Citibank because Citibank acted at all times in good faith and without actual knowledge of any violation of Section 12(2) of the Securities Act of 1933 by Topper, Orenstein, Hayden Stone or Bernstein-Macauley, and Citibank did not directly or indirectly induce any such violation.

AS AND FOR A NINTH AFFIRMATIVE
DEFENSE, DEFENDANT CITIBANK
ALLEGES THAT:

99. Counts Four and Six of the complaint fail to state a claim upon which relief can be granted against Citibank because a cause of action pursuant to Section 12(2) of the Securities Act can be asserted only by a purchaser of securities against the person who offers or sells securities to him.

AS AND FOR A TENTH AFFIRMATIVE
DEFENSE, DEFENDANT CITIBANK
ALLEGES THAT:

100. Count Five of the complaint fails to state a cause of action upon which relief can be granted against Citibank because Citibank acted at all times in good faith and without actual knowledge of any violation of Section 17(a) of the Securities Act by Topper, Orenstein, Hayden Stone or Bernstein-Macauley, and Citibank did not directly or indirectly induce any such violation.

AS AND FOR AN ELEVENTH AFFIRMATIVE DEFENSE, DEFENDANT CITIBANK ALLEGES THAT:

101. Count Nine of the complaint fails to state a claim upon which relief can be granted against Citibank because Citibank acted at all times in good faith and without actual knowledge of any act having been committed constituting fraud and deceit upon Pension Fund or Connecticut Mutual, and Citibank did not directly or indirectly induce any such act.

AS AND FOR A TWELFTH AFFIRMATIVE DEFENSE, DEFENDANT CITIBANK ALLEGES THAT:

102. Counts Three and Six of the complaint fail to state a claim upon which relief can be granted against Citibank because they fail to state any facts indicating that Citibank controlled Topper.

AS AND FOR A THIRTEENTH AFFIRMATIVE DEFENSE, DEFENDANT CITIBANK ALLEGES THAT:

103. Counts Eight, Nine and Eleven of the complaint fail to state a claim for exemplary damages.

AS AND FOR A FOURTEENTH AFFIRMATIVE DEFENSE, DEFENDANT CITIBANK ALLEGES THAT:

104. Plaintiffs do not have a right to a jury trial with respect to Count Eight of the complaint, because the claim therein against Citibank based upon unjust enrichment is in the nature of an equitable claim.

WHEREFORE, Citibank demands judgment dismissing the complaint, together with costs and disbursements and such other and further relief as the Court may deem just and proper.

New York, New York
March 28, 1974

SHEARMAN & STERLING

By W. Foster Wollen
A Member of the Firm
Attorneys for Defendant
First National City Bank
53 Wall Street
New York, New York
(212) 483-1000

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

- -x

UNITED STATES STEEL AND :
CARNEGIE PENSION FUND, INC.,
et al., :

Plaintiffs, : 74 Civ. 391 (WK)

-against- : AMENDED ANSWER

HENRY ORENSTEIN, et al., :

Defendants. :

- -x

Defendant First National City Bank ("Citibank"), by its attorneys, Shearman & Sterling, amends its answer to the complaint herein to add the following:

AS AND FOR A FIFTEENTH AFFIRMATIVE DEFENSE, DEFENDANT CITIBANK ALLEGES THAT:

105. On information and belief, on or about February 13, 1976, plaintiffs gave releases to defendants Shearson Hayden Stone, Inc., Bernstein-Macaulay, Inc., Roger S. Berlind, Sanford I. Weill and Henry Orenstein and stipulated the discontinuance, with prejudice, of this action against such defendants.

106. As a result, plaintiffs' claims against Citibank are reduced to the extent of the amount stipulated in such releases, or in the amount of the consideration paid for such releases, or in the amount

of the released defendants' equitable shares of plaintiffs' damages, whichever amount is the greatest.

Dated: New York, New York
February 17, 1976

SHEARMAN & STERLING

By____________________________
A Member of the Firm
Attorneys for Defendant
First National City Bank
53 Wall Street
New York, New York
(212) 483-1000

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

U.S. District Court
Filed
SEP 21. 1976
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LESTER CONNELL, JOHN CANARIO, LEO R. CHURCH, MORRIS A. FELDMAN, JOSEPH FORZANO, WILLIAM HENNESSEY, RAYMOND MARKEY, FRANK SCOTTO, FRANK E. WOLF and BENJAMIN YOUNG, as Trustees of the Local 816 Labor and Management Pension Trust Fund,

Plaintiffs,

- against -

BERNSTEIN-MACAULAY, INC., et al.,

Defendants.

Consolidated Index No.
72 Civ. 3272
(WK)

JUDGMENT

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UNITED STATES STEEL and CARNEGIE PENSION FUND, INC., CONNECTICUT MUTUAL LIFE INSURANCE COMPANY and NATIONAL BANK OF COMMERCE OF DALLAS as Trustee of the Omega-Alpha, Inc. Pool Trust,

Plaintiffs,

- against -

HENRY ORENSTEIN, et al.,

Defendants.

74 Civ. 391

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These actions came on for trial before the Court, Honorable Whitman Knapp, District Judge, presiding, and the evidence adduced by the parties having been heard and the Court having rendered and filed its opinion, and having made and filed findings of fact and conclusions of law, all dated August 3, 1976,

IT IS ORDERED AND ADJUDGED that the plaintiffs herein take nothing, that the actions be dismissed, with prejudice, on the merits as to defendant Citibank, N.A. (formerly known as First National City Bank) and that defendant Citibank, N.A. recover its costs of action to be taxed from plaintiffs.

Dated at New York, New York this 16 day of ~~August~~ September, 1976.

Whitman Knapp
~~Clerk of the~~ Court
USDJ

~~Approved:~~

~~United States District Judge~~

Judgment Entered 9/21/76

Raymond F Burghardt

Clerk

Opinion of the District Court

Knapp, D.J.

Plaintiffs[1] are a group of financial institutions which on September 28, 1971 invested $5,250,000 in a private placement of Topper Corporation convertible debentures, only to have their investment evaporate within two years upon Topper's bankruptcy. Defendant First National City Bank ("Citibank" or the "Bank") was not directly involved in the placement. However, through its commercial finance (i.e. factoring) department it had over the years been Topper's principal banker, having responsibility for administering an outstanding loan of some twenty million dollars.[2] Of this loan about five million was deemed by the Bank to be an "over advance", i.e. in excess of the amount permissible in relation to Topper's accounts receivable which had been pledged as security. The proceeds of the private placement were used to reduce this over advance.[3] Through another of its departments Citibank also had an advisory investment account with plaintiff United States Steel and Carnegie Pension Fund (the "Pension Fund" or the "Fund") which was the "lead" institution in the private placement and which invested $3,000,000 of its own in the disastrous venture. On August 27, 1971 one Henry Thompson, an investment manager for the Pension Fund, had a telephone conversation with one Edward Waldman, senior vice president in charge of Citibank's factoring department, the results of which conversation were ultimately communicated to the other plaintiffs.

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[1] In 74 Civ. 391, the plaintiffs are United States Steel and Carnegie Pension Fund Inc., Connecticut Mutual Life Insurance Company and National Bank of Commerce of Dallas (as trustees of the Omega-Alpha, Inc. Pool Trust). In 72 Civ. 3272 the plaintiffs are Lester Connell, John Canario, Leo R. Church, Morris A. Edelman, Joseph Forzano, William Hennessey, Raymond Markey, Frank Scotto, Frank E. Wolf and Benjamin Young as trustees of the Local 818 Labor and Management Pension Trust Fund.

The defendants originally included Shearson Hayden Stone, Inc., Bernstein-Macaulay, Inc., Sanford I. Weill, Roger S. Berlind (the Hayden Stone defendants), Henry Orenstein and Peter L. Bernstein. After extensive pre-trial preparation ably conducted by Magistrate Schreiber, the various claims against some were settled, while others were left to be determined in separate trials.

The Pension Fund took the lead in this litigation, there being no serious contention that any other plaintiff would have a cause of action if the Pension Fund should fail. Accordingly, this opinion will address itself solely to the claim of the Pension Fund.

[2] A large proportion of this $20,000,000 represented Citibank's own money, the balance being advanced by a group of other banks on whose behalf it was managing the account.

These actions (consolidated for trial) are brought pursuant to §10b of the 1934 Securities Exchange Act and §17a of the 1933 Securities Act, on the theory that plaintiffs were misled by the Thompson-Waldman telephone conversation and that such misleading gave rise to actionable fraud under the sections cited. The Pension Fund, relying upon its investment contract, also claims that Citibank violated its fiduciary duty, and therefore asserts a pendent claim of breach of trust. After a three week bench trial the court tentatively announced its conclusion that plaintiffs had failed to sustain any cause of action, and that their complaints should be dismissed. Having reviewed the exhaustive briefs and the thoroughly documented findings of fact submitted by the parties, we see no reason to change our conclusion.[4]

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[3] Although the over advance was initially reduced by the private placement, the Bank continued making advances and by late December the over advance was greater than it had been at any time the private placement was under discussion.

[4] At the close of the trial, the court set forth several tentative conclusions as to the facts (Tr. 1378-92) and went into considerable detail with respect to its observations as to the credibility (i.e.

The Facts

Topper was one of the more successful toy manufacturers and had had a phenomenal growth in the late 60's. It was run by one Henry Orenstein who was a brilliant entrepreneur. Success or failure in the toy manufacturing business depended upon the manufacturer's success in inducing distributors and important retailers such as Kresge and Sears Roebuck to stock large quantities of toys and have them "on the shelf" ready for the Christmas season. Orenstein devised various methods to entice retailers and distributors to stock Topper toys. All these methods ultimately resulted in the retailer or distributor being able to obtain Topper merchandise—or have it warehoused at Topper expense—upon conditions under which the retailer or distributor paid Topper only when and if the public ultimately bought the toys. The beauty of this arrangement—from the distributor and retailer's point of view—was that he could without risk to himself have a vast array of Topper toys available to be sold, just as if he had ordered them on consignment.

Shrewdly suspecting that secured creditors and other investors would find these arrangements less attractive than did the retailers, Orenstein arranged Topper books and records so that all transactions were reflected as final

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factual accuracy of witnesses. (Tr. 1382-90). With the exception of certain speculation concerning the effect of Citibank's failure to call the witness Jeffers (e.g. Tr. 1379-82)—which speculation was rendered moot when Jeffers was produced at the direction of the court (see Tr. 1506)—we adhere to those findings and observations. In addition, we have carefully reviewed the comprehensive findings submitted by the parties (776 in all), indicating as to each one whether it is accepted, rejected or modified (see appendix to this opinion). This statement of facts will therefore be confined to a broad outline of the relevant evidence.

sales to its abundantly solvent customers whose shelves were burgeoning with Topper toys. Indeed, the customers routinely returned auditors' letters confirming the sales involved.

These arrangements worked to everyone's benefit so long as retail sales were brisk. In 1971, however, such sales turned sluggish and Topper's past due accounts receivable began to rise rather precipitously. Citibank, which kept careful watch over Topper accounts receivable, instantly became aware of this situation and urged Topper to bring pressure on its customers to pay down their accounts. Orenstein agreed to do this if the Bank insisted, saying that the accounts could easily be cleaned up in a matter of weeks. However, he strongly advised against such a course on the ground that it would put Topper at a competitive disadvantage with more lenient manufacturers. Since Citibank was confident of the customers' credit it accepted Orenstein's judgment and did not press for immediate collection. It was not until December of 1971, three months after the private placement, that Citibank began to discover that the accounts were not only uncollectible but non-existent.

Topper first came to plaintiff Pension Fund's attention in the spring of 1970 when a Hayden Stone official mentioned to Henry Thompson that Hayden Stone was underwriting an issue of Topper stock. Thompson decided that the Fund was not then interested in investing in the company. However in July, 1971, when Hayden Stone suggested the possibility of a private placement of debentures convertible into equity, Thompson thought this might be an appropriate investment for the Fund.

Thompson went through the normal routine of investigation in preparation for such an investment. Among other things he conferred with Hayden Stone representatives; he visited Topper's offices, where he spoke to, among others, Orenstein and one Jack Rose, Topper's chief financial officer; and he checked trade and bank references. None of these investigations brought to light the condition of the accounts receivable. He came close to such a discovery during a visit to Topper's offices. He there asked Rose to let him see some of the actual documents concerning receivables. However, that question came up just before lunch. Rose impressed upon Thompson the importance of their luncheon appointment with Orenstein, and the subject was never again mentioned.

In his check of trade references, Thompson received glowing accounts of Topper's imaginative management, with special emphasis upon Topper's understanding of distributors' and retailers' problems and its willingness—in contrast with its less imaginative competitors—to accommodate its customers by taking back unsold merchandise. Thompson did not inquire of the trade references whether this policy included letting them have merchandise on consignment.

This lawsuit, however, is concerned with Thompson's check of bank references, which involved his August 27 telephone conversation with Waldman.

In the course of his meetings with Topper personnel, Thompson had learned that Topper was principally financed through the non-notification factoring of its accounts receivable, that it had a secured credit line with a group of banks of which Citibank was the leader, and that the person actually in charge of managing the account was Edward Waldman, the Citibank senior vice president in charge of its commercial finance department. Thompson received Topper's permission to consult Waldman.

Thompson took this information back to his superior, one Henry Molé, and they decided that the best way to contact Waldman was through Walter Jeffers, another senior vice president who had for years been the liason [*sic*] with respect to the Fund's investment account and who had also been in charge of United States Steel Corporation's very substantial commercial account with the Bank. Thompson accordingly called Jeffers, who arranged to have Waldman return the call.[5]

There ensued the conversation upon which this lawsuit is based.[6] In essence, Waldman told Thompson that—from his point of view as a secured lender—Topper's was a wholly satisfactory account and that he neither knew of nor foresaw any problem. In response to Thompson's request for investment advice, Waldman said he was in no position to give any.[7] When Thompson reported this conversation to Molé, the latter told him that he had had no business asking Waldman for investment advice.

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[5] The actual testimony was quite different from the foregoing. It was the testimony of both Thompson and Molé that—although Thompson had ascertained Waldman's identity from Topper and although there was no reason for them to believe that Jeffers had any familiarity with the Topper account—they nonetheless decided to have Thompson call Jeffers and ask his unguided advice as to the best Citibank person to consult with respect to investing in Topper. For reasons indicated at trial (Tr. 665-6) we reject this testimony as incredible, and have reconstructed the events as we believe they must have occurred.

[6] In the post-trial arguments, counsel for plaintiff Lester Connell advanced the theory that, regardless of the Thompson-Waldman conversation, the Bank is liable to plaintiffs because it benefited from the private placement (Tr. 1393-97). Unless ***Affiliated Ute Citizens (infra)*** be deemed to support this proposition, no authority was ever cited. The argument has apparently been abandoned in the post-trial briefs.

[7] At trial the plaintiff—through testimony of Thompson and cross-examination of Waldman—attempted to create the impression that this conversation was both lengthy and involved. We have concluded that nothing of any consequence was said in the course of the conversation which is not reflected in plaintiffs' Exhibit 1397 [*sic:* 1379], the contemporaneous report that Thompson made to his superior, Molé.

The ultimate decision whether to invest in the private placement was not made by Thompson or Molé but by the Fund's Committee on Finance. Thompson, under Molé's supervision, prepared a memorandum to that Committee, which set forth the facts and considerations they deemed relevant to its decision (plaintiff's Exh. 1370). This memorandum did not mention Citibank or any special relationship the Fund may have had with that institution. It simply said that "retail trade and banking checks have been favorable".[8]

Based on the evidence of which the foregoing is a rough summary, the court specifically finds (in addition to the Findings suggested by the parties and adopted by us) that:

(1) Waldman acted in good faith in his conversation with Thompson.[9]

(2) Neither Waldman, Jeffers nor any other officer or employee of the Bank (or the Bank itself) had any

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[8] The fact that the Finance Committee may have been unaware of any Citibank involvement is of course irrelevant. However, the circumstance that Molé and Thompson did not deem it worth mentioning strongly supports our view that they did not then think of themselves as having asked the Bank for advice pursuant to the investment contract or any other special relationship, but that they were simply making routine "trade and banking checks".

[9] Plaintiffs spent much of the trial in an ultimately unsuccessful attempt to persuade the court that Waldman had lied in telling Thompson that he foresaw no problems. Alternatively they urge that he was grossly negligent in not realizing that "problems" were indeed foreseeable. That, it seems to us, might be relevant were this a derivative suit against Waldman on behalf of the Bank. Even in such a suit we would be contrained [*sic*] to find, in light of the expert testimony offered at trial and accepted by us, that plaintiffs had failed to sustain their burden of proof.

conceivable motive to mislead Thompson or the Fund. Any benefit the Bank might have received from the private placement (even if not short-lived as it turned out) would have been insignificant compared to the risk of jeopardizing not only the Bank's investment account with the Fund but its far more substantial commercial account with United States Steel Corporation.

(3) In making the call to Jeffers neither Molé nor Thompson (nor their employer, the Fund) was seeking investment advice pursuant to the advisory contract or any special relationship the Fund had with the Bank.

(4) Neither Jeffers nor Waldman nor anyone connected with the Bank either believed or had reason to believe that the Bank was giving or had been asked to give investment advice pursuant to the investment advisory contract or any other special relationship between the Bank and the Fund.

(5) Neither the Bank nor any of its officers or employees either knew or had reason to know of any misrepresentation that Topper may have made to the Fund or to any other plaintiff.

THE LAW

Upon our view of the facts, there really is no law to discuss. However, we shall briefly consider some of plaintiffs' major contentions.

To establish its basic premise that the Bank owed a duty to the investors in the private placement, plaintiffs principally rely upon *Affiliated Ute Citizens* v. *United States* (1972) 406 U.S. 128. For present purposes, we accept plaintiffs' statement of the essence of that decision, as summarized in the Ninth Circuit opinion of *White* v. *Abrams* (1974) 495 F.2d 724. According to plaintiffs the following factors are relevant (Plaintiffs' Post Trial Memorandum at p. 32):

(a) "the activity of the defendants" in relation to the securities transaction in question (495 F.2d at 731);

(b) "the benefit the defendants derived from the sale of the stock" (*id.*);

(c) "the access the defendants had to the undisclosed information as compared with the access of the plaintiffs" (*id.*);

(d) "the relationship of the defendant to the plaintiff" including "the defendant's awareness of whether the plaintiff was relying upon their relationship in making his investment decisions" (*id.* at 735).

Circumstances relevant to factors (a) and (b) have not been dealt with in the foregoing summary. However our adoption of Citibank's proposed Findings Nos. 18-23, 28-38, 61 and 115 eliminates these factors. It appears from those Findings that the Bank played no part in Topper's management other than to advise on what terms it was willing to continue its loans, and that any benefit the Bank may have gained from the use of the private placement to reduce its outstanding balances was quickly dissipated by new loans made in a continuing course of business.

With respect to factor (c) the critical information which Topper withheld from plaintiffs was that its accounts receivable were sham.[10] That information was as accessible to plaintiffs as to the Bank, if not more so. Just as the Bank could have discovered the fraud by insisting upon seeing the actual documentation, so could have the plaintiffs. Furthermore, since the accounts were on a non-notification basis, the Bank was precluded from making direct approaches to Topper customers, an avenue which was clearly open to plaintiffs.[11]

Factor (d) is eliminated by our Findings (3) and (4) above.

Plaintiffs also contend that the Bank may be held liable as an aider and abettor of Topper's conceded fraud. Any such contention is foreclosed by our Finding (5) above.

That same Finding also forecloses reliance upon plaintiffs' final theory that the Bank was a controlling person of

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[10] At the close of trial, counsel for plaintiffs strenuously argued that the critical fact was not the invalidity of the accounts, but Topper's easy practices with respect to returns (Tr. 1419). That argument has now been abandoned. Plaintiffs continue to urge that the Bank (i.e. Waldman) should have alerted plaintiffs (i.e. Thompson) to the fact that past due accounts were growing at an "alarming" rate. The difficulty with both arguments is the same. Waldman saw nothing alarming either in the easy return policy or in the past due accounts. He had been convinced by Orenstein that both were sound business practices. Moreover, believing that substantial and knowledgeable retailers such as Kresge and Sears had committed their credit to the purchases involved, the Bank was entitled to assume that these retailers had confidence that the merchandise would ultimately be sold. In any event there was no occasion—in the brief conversation described in Plaintiffs' Exhibit 1379—for Waldman to get into any philosophical discussion of Topper's business practices.

[11] Thompson could, by appropriate questions to his trade references, have ascertained practically all the facts set forth in plaintiffs' Findings 57, 60, 62-69 and 80. Apparently one potential investor, the Princeton University Endowment Fund, was dissuaded from participating in the private placement as a result of such an inquiry. (Tr. 705).

Topper. Even if Citibank were a controlling person, it would not be liable for its controllee's unsuspected frauds. *Gordon* v. *Burr* (2d Cir. 1974) 506 F.2d 1080; *Lanza* v. *Drexel & Co.* (2d Cir. 1973) 479 F.2d 1277, 1299. Furthermore, our acceptance of Citibank findings 18-23, 28-38, and 115 establish that the Bank was not in fact such a controlling person.

Accordingly plaintiffs' complaints are dismissed. Let defendant submit judgment on five (5) days notice.

Dated: New York, New York
August 3, 1976
[As supplemented on
September 15, 1976.]

/s/ WHITMAN KNAPP

Whitman Knapp
U.S.D.J.

Appendix to the Opinion of the District Court

FINDINGS OF FACT

(as respectively submitted by the parties)

Except as indicated below, all findings proposed by the parties are adopted by the court.[*] In acting upon the submitted findings the court expresses no opinion as to the relevance or materiality of any of them. It is our view that each party should—for purposes of pressing or resisting an appeal—know the trial court's conclusion as to any fact such party considers important. We have therefore rejected or modified only such findings as we deem inaccurate, misleading, or not based on credible evidence. No attempt has been made to appraise any statement of fact set forth in a footnote. The adoption or rejection of a particular finding neither adopts nor rejects its footnote.

Several of the proposed findings purport to state the views or conduct of persons not parties to this law suit. The adoption, rejection or modification of any such finding is not intended to effect the rights or interests of any such person.

With respect to those findings purporting to be supported in whole or in part by depositions and documents not referred to at trial, we have—since neither party has suggested that such material substantially affected the thrust of the evidence actually discussed during the trial (see Tr. 1378)—accepted them if they appear to be in accord with the facts so far as known by us, but we have not necessarily verified the individual references.

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[*] Editor's Note: contained herein at pages A41-A348 are the Findings of Fact submitted by the respective parties to the appeal, as modified and adopted by the District Court.

Findings Proposed by the Pension Fund

1. *Finding 7(a)* is amended by deleting the words "and reviewed Topper's current financial condition with a senior lending officer at Citibank" on the ground that they do not accurately describe the Thompson-Waldman conversation.

2. *Finding 9* is amended by replacing the words "Price Waterhouse" in the first line with "Ira Carl Weiss, a certified public accountant who had been employed by Price Waterhouse since 1966". *Findings 86, 123, 134, 152, 156, 158, 160, 174, 177, 184, 185, 190* are amended by inserting the words "Mr. Weiss of" before the words "Price Waterhouse" wherever they appear.

3. *Finding 19* is amended by deleting the last five and one-half lines beginning with the words "and asked for" as inconsistent with the court's conclusions.

4. *Finding 20* is amended by deleting the words "to this request" in the first line and by substituting in the last line the words "with the Topper account" for the words "at Topper".

5. *Finding 27(c)* is rejected. The facts stated, although asserted by Thompson at trial, are not supported by his contemporaneous memorandum.

6. *Finding 40* is rejected on the ground that, although it is a correct statement of Mr. Inglis' testimony, the court is unwilling to confirm the accuracy of his observations.

7. *Findings 89, 91, 92* are rejected as overstatements of the evidence.

8. *Finding 94* is amended by eliminating the first sentence and the word "thus" at the beginning of the second sentence.

9. *Finding 97* is amended by eliminating the first line.

10. *Finding 100* is amended by eliminating the first sentence.

11. *Finding 101(d)* is amended by substituting the words "had not been paid by November 22 of that year" for the words "were never paid" in the third line.

12. *Finding 125* is amended by substituting the word "discontinued" for the words "was forced to discontinue" in the first and second lines.

13. *Finding 133* is amended by substituting the word "Siegel's" for the word "Citibank's" in the second line.

14. *Finding 137* is amended by inserting the words "a partner of" before the words "Arthur Young" in the second line on the ground that—in contrast with the situation presented in Finding 163—the witness was expressing his own opinion rather than describing an Arthur Young worksheet.

15. *Finding 217, 218, 219, 220, 225, 229, 230, 231, 234* are rejected on the ground that they rest exclusively on the deposition testimony of Rose and/or Orenstein, there being nothing in the evidence to suggest that either of them is worthy of belief.

16. *Finding 222* is amended by deleting the words "pursuant to Citibank's direction" from the tenth line.

17. *Finding 226* is amended by substituting the word "an" for the words "the most poignant" in the second sentence.

18. *Finding 232* is amended by deleting the first sentence and the word "thus" from the beginning of the second sentence.

19. *Finding 235* is amended by deleting the first three lines and by inserting at the beginning of the fourth line the words "In March, 1971".

20. *Finding 236* is rejected as not supported by the testimony cited.

21. *Finding 237* is amended by deleting the words "In addition" from the first line and the word "arbitrarily" from the seventh line.

22. *Finding 238* is amended by deleting the first two lines and by inserting the words "Citibank insisted that Topper 'notify'" at the beginning of the third line.

23. *Finding 247* is rejected as not supported by the record references.

24. *Finding 248* is rejected as unclear.

25. *Finding 249* is amended by deleting the words "in point of fact" from the first line.

26. *Finding 252* is rejected as unsupported by the citations to the record.

27. *Finding 258* is amended by deleting the word "disturbing" from the third line.

28. *Finding 259* is amended by eliminating the words "most significantly" from the first line.

29. *Findings 260 and 261* are rejected, since the testimony cited had no necessary relationship to Citibank.

30. *Finding 262* is rejected as purporting to be supported by findings previously eliminated.

31. *Finding 265* is rejected as argumentative and unsupported.

32. *Finding 266* is rejected as unclear.

33. *Finding 267* is amended by deleting the first sentence, and by deleting the last sentence on the ground that it appears to be unrelated to the record citation.

34. *Finding 268* is amended by substituting the figure "6.5" for "6.3" in the fourth line and by substituting the figure "1,435,920" for "1,235,920" in the fifth line.

35. *Finding 270* is rejected as speculative.

36. *Finding 273* is rejected on the ground that the evidence cited does not establish that Manufacturers Hanover was ever called upon to make a decision.

37. *Finding 280* is amended by striking all but the first sentence, since the evidence cited is insufficient to establish the existence of a bank policy.

38. *Finding 285* is amended by deleting the first sentence as attributable excusively to Rose, and by substituting the word "Siegel" for "Ford Motor" in the seventh line.

39. *Finding 288* is amended to substitute the word "Siegel" for "a Ford Motor officer" in the seventh line.

40. *Finding 291* is revised so that its second sentence reads as follows:

> "On this occasion, in a step which worked to reduce Citibank's financial commitment to Topper, Citibank agreed to share its first security interest under the Finance Agreement with Ford Motor Credit Company on a *pari passu* basis to the full extent of its $7 million loan."

41. *Finding 296* is amended by striking the first sentence and the words "not to Topper but" from the second sentence.

42. *Finding 298* is rejected on the ground that the court believes that the approach to Citibank was made because of its position as secured lender to Topper, the Pension Fund's relation to the bank affecting only the method of approach.

43. *Findings 300 and 301* are rejected as inconsistent with the court's conclusions drawn from the testimony, as indicated in footnote 5 to the opinion.

44. *Finding 302* is rejected on the ground that although properly quoted from the transcript it is not appropriately stated as a finding for the court to make.

45. *Finding 303* is amended by deleting the first sentence and the words "in fact" at the beginning of the second sentence on the ground that there is no evidence that Siegel took any action with respect to the prospectus in the course of his employment.

46. *Finding 304* is rejected as inconsistent with the court's conclusions.

47. *Finding 305* is amended by deleting the words "upon learning this" from the first line, and by rephrasing

the last sentence to read, "Jeffers then asked Waldman to call Thompson."

48. *Findings 308 through 314* are rejected, as the court is unwilling to go beyond Thompson's contemporaneous memorandum of the conversation.

49. *Finding 315* is amended by deleting the first five lines and by replacing them with the following words:

    "With respect to the conversation Mr. Waldman testified as follows:"

50. *Finding 316* is amended by deleting the final clause, commencing with the words "which corroborates".

51. *Finding 318* is rejected because the testimony and diary entries satisfy the court that Waldman did not hear from Provine until after his conversation with Thompson.

52. *Findings 322 through 361,* under the headings, "Waldman's Claim that he believed there were no 'problems' on August 27 lacks credibility" and "the Pension Fund reasonably relied on the Citibank report in connection with the Private Placement" are rejected as argumentative and in large part contrary to the conclusions at which the court has arrived.

Findings Proposed by Citibank

1. *Finding 28* is rejected on the ground that it is supported only by the deposition testimony of Rose (see ¶15 *supra*).

2. *Finding 33* is modified so that the second sentence begins "At that time, Citibank was advised that, subject to the bank's consent, Ford Motor Credit's advances . . . ."

3. *Finding 47* is modified so that the second sentence reads, "The Lending Banks believed that they were adequately secured." In line 8, substitute "appeared to be" for "was".

4. *Finding 90* is modified by eliminating the word "no" with which it begins, replacing it with "It has not been established that any".

5. *Finding 228* is modified to eliminate all but the first two sentences on the ground that the portion eliminated is inconsistent with the court's own view.

6. *Finding 230* is eliminated as inconsistent with the court's view of the evidence.

7. *Finding 283* is modified so that the last clause reads "nor did Citibank purport to give investment advice to the Pension Fund."

8. *Findings 410-12* are rejected on the ground that we are unwilling to rely upon the apparently self-serving deposition testimony of Topper employees.

CONCLUSIONS OF LAW

Plaintiffs have proposed no formal conclusions of law, while Citibank has submitted thirty-eight. We have not passed upon any of those submitted, as we feel that our opinion adequately reflects our views as to the law.

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FINDINGS OF FACT
ADOPTED BY THE DISTRICT COURT
WHICH WERE PROPOSED BY PLAINTIFFS

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Findings of Fact

I.

THE PRIVATE PLACEMENT

A.

Background

P1. This action arises out of the private placement of $5,250,000 in convertible subordinated notes of Topper Corporation ("Topper") on September 28, 1971 (the "Private Placement"). Topper was engaged in the business of manufacturing and marketing toys for boys and girls (CB ADM 11).

P2. Plaintiff United States Steel and Carnegie Pension Fund, Inc. (the "Pension Fund")[1] purchased $3 million of the Topper securities (CB ADM 3); plaintiff Connecticut Mutual Life Insurance Company ("Connecticut Mutual") purchased $1 million (CB ADM 6); and plaintiff National Bank of Commerce of Dallas (the "Dallas Bank") bought $250,000 in its capacity as trustee for the Omega-Alpha, Inc. Pool Trust (CB ADM 8).

P3. The day following the Private Placement, on September 29, 1971, Topper turned over to defendant First National City Bank ("Citibank") the entire proceeds of the Private Placement (CB ADM 90). Citibank, which had acted as Topper's lead commercial banker since 1966 (CB ADM 17), received the proceeds in repayment of a "bridge" loan extended one month earlier on the express condition that Topper effect the Private Placement and remit its proceeds to Citibank (CB ADM 227).[2]

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[1] The Pension Fund invests and reinvests funds in its charge in order to insure availability of monies sufficient to provide pension benefits to, as of the end of 1971, approximately 68,000 pensioners, as well as roughly 180,000 then present employees who, with the exception of certain coal miners, "were participants" (*Mole Tr.* 639-40). Again as of the end of 1971, the average pension paid ran "[a]pproximately $300 a month" (*id.* at 640A) for a period of "[a]bout 17 years" (*id.* at 640).

P4. Within three months of the Private Placement, on December 17, 1971, Topper announced that it would suffer a significant loss of $10 to $15 million for the fiscal year ending December 31, 1971 (PX 601). In fact the loss suffered by Topper was far greater, aggregating $37.2 million for the seventeen-month period ending May 31, 1972 (PX 1101 at 3), although management was "certain that a large segment of that loss should be more properly reflected in the 1970 financials" (*Clarke Dep.* 111).

P5. Topper never recovered from these misfortunes, and on May 7, 1973, was declared bankrupt (CB ADM 202). As a result, the $4,250,000 of Topper notes sold plaintiffs in the Private Placement are worthless (CB ADM 203).

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[2] See Plaintiffs' Findings P271 - P272, P274 - P289, *infra* at A173-A178.

B.

Plaintiffs' View of Topper Prior to the Private Placement

P6. Prior to the Private Placement each plaintiff received a memorandum bearing the date July 1971 (PX 462), which included Topper's April 29, 1971 prospectus (the "Private Placement Memorandum") (*Thompson Tr.* 389; *Hieronymus Tr.* 574). The Private Placement Memorandum served to update the April 29, 1971 prospectus, and together purported to describe the financial condition and material business practices of Topper.

P7. In addition to receiving the Private Placement Memorandum and the April 29, 1971 prospectus, the Pension Fund and Connecticut Mutual made certain independent inquiries to verify and supplement this information as part of the consideration which preceded their decision to participate in the Private Placement:

(a) Pension Fund officers met with Topper management on three occasions prior to the Private Placement,[3] talked with two major toy customers,[4] spoke with an outside director of Topper,[5] called a toy analyst in the securities industry,[6] and checked with a representative of Children's Television Workshop which had recently awarded Topper the right to manufacture the Sesame Street line of toys;[7] and

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[3] See *Thompson Tr.* 393-401, 405-06, 416-19, 422, 424-25, 450-52; *Mole Tr.* 671-77; PX 1371, 1372, 1378.

[4] See *Thompson Tr.* 406-12; PX 1375, 1376.

[5] See *Thompson Tr.* 412-15; PX 1377.

[6] See *Thompson Tr.* 420-21; PX 1373.

[7] See *Thompson Tr.* 405-06; PX 1374.

(b) likewise, Connecticut Mutual took part in a full day meeting with Topper management,[8] had numerous telephone conversations on Topper with its investment banker,[9] spoke to two toy customers of Topper,[10] and kept abreast of the Pension Fund's ongoing investigation as well.[11]

(i) *Plaintiffs' View of Topper's Financial Condition*

P8. Initially Topper was portrayed as a financially stable company which had overcome one turbulent period in the mid-1960's, had shown steadily increasing profits from continuing operations ever since, and was about to report record profits for 1971 (PX 1372 at 2-3; PX 1370 at 1-2, 4; *Thompson Tr.* 393; *Hieronymus Tr.* 605; PX 1417 at 1-2, 4-6; PX 1423 at 8-11). Thus following substantial losses in 1965 and 1966, Topper's Consolidated Statement of Operations, certified by Arthur Young & Company ("Arthur Young") and distributed to plaintiffs as part of the Private Placement Memorandum, showed marked financial improvement (*Hieronymus Tr.* 578):

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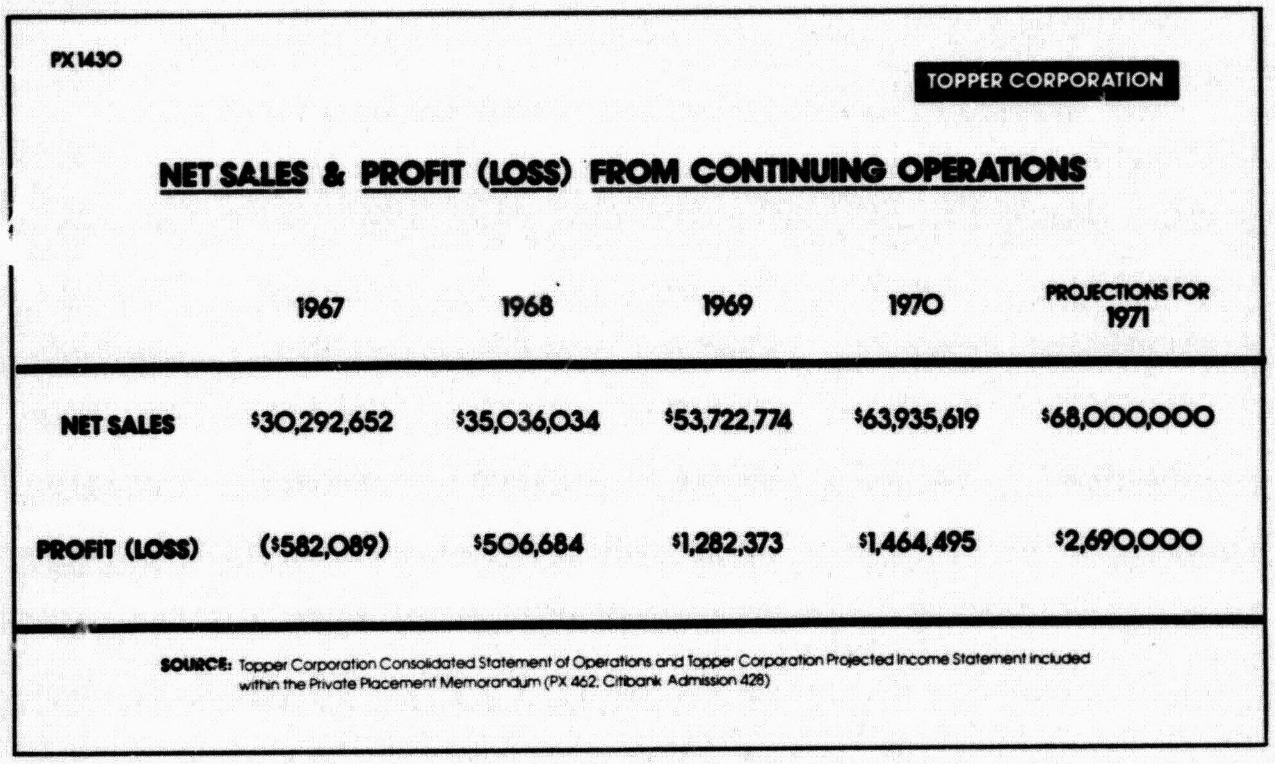
[8] See *Hieronymus Tr.* 580-97; PX 1417.

[9] See *Hieronymus Tr.* 576-80, 597-99, 606-09, 611, 613-14; PX 1419.

[10] See *Hieronymus Tr.* 600-03; PX 1421, 1422.

[11] See *Hieronymus Tr.* 597-98, 607, 609, 611, 614; PX 1419 at 2.



PX 1430

TOPPER CORPORATION

NET SALES & PROFIT (LOSS) FROM CONTINUING OPERATIONS

	1967	1968	1969	1970	PROJECTIONS FOR 1971
NET SALES	$30,292,652	$35,036,034	$53,722,774	$63,935,619	$68,000,000
PROFIT (LOSS)	($582,089)	$506,684	$1,282,373	$1,464,495	$2,690,000

SOURCE: Topper Corporation Consolidated Statement of Operations and Topper Corporation Projected Income Statement included within the Private Placement Memorandum (PX 462; Citibank Admission 428)

P9. According to Ira Carl Weiss, a certified public accountant who had been employed by Price Waterhouse since 1966, this financial information reflected a company which had enjoyed a significant increase in sales over the past five years (*Weiss Tr.* 133), and "a very steady, safe type of increase" in net profit from continuing operations, one that "gave a picture of stability" to Topper's operations (*id.* at 133-34; PX 1370 at 1; PX 1423 at 11).

P10. The favorable financial trends reflected in Topper's audited financial statements continued in those interim financial statements for 1971 distributed to plaintiffs (PX 1420, 1459, 1460, 1378). Thus:

(a) Topper's April 29, 1971 prospectus reported that as a result of Topper's "ability to ship low priced merchandise which was not available during the spring of 1970", net sales of $4.9 million for the first quarter of 1971 were more than double the amount for 1970, and that Topper had suffered a net loss in this traditionally slow quarter of only $398,000 compared with a net loss of $1,039,959 in 1970 (PX 462, Exh. 1 at 9); and

(b) for the six-month period ending June 30, 1971, Topper reported that net sales had increased nearly 25%, from $15.6 million in 1970 to $19.3 [million] in 1971; more significantly, Topper's net profit before taxes had risen by $1.3 million during the first six months, from a net loss of $751,000 in 1970 to a net profit of $590,000 in 1971 (PX 2 at 4; see PX 1423 at 8-9).

P11. The successful year reflected in the interim financial statements distributed to plaintiffs was projected to continue for the remainder of 1971 (PX 462 at 24). Among other things, these projections estimated net sales for 1971 of $68 million and a net profit from continuing operations of $2.7 million (PX 1430; PX 1370 at 4; PX 1423 at 8-9); in addition, the projections estimated that by year-end 1971, Topper would have a net cash surplus of $27.5 million (PX 462 at 24; *Thompson Tr.* 391).

P12. Concerning the reliability of these projections, the Private Placement Memorandum stated that it was Topper's "experience that overall sales may be projected with a reasonable degree of accuracy" (PX 462 at 16; PX 1417 at 1; PX 1423 at 9-10). Beyond this, Connecticut Mutual was informed by Mr. Downs, Topper's Executive Vice President, that "with the orders that they had received it looked like the $68 million" in projected sales "was going to be exceeded" (*Hieronymus Tr.* 581). "And Henry Orenstein said at this point in time of the year he had never been wrong in his analysis of the projections" (*id.*).

P13. For its part, the Pension Fund requested that Topper prepare a projection of minimum operations to determine Topper's break-even point for 1971 (PX 1378 at 2; PX 1419 at 1). In response, Topper prepared and distributed to the Pension Fund and to Connecticut Mutual a "fail-safe" set of projections which showed that, although Topper was currently projecting a sales volume of $68 million for the year and "an operating profit (before extraordinary depreciation and amortization) of $6,673,000" it would nonetheless be able to break even in 1971 with sales of only $56 million (PX 1380 at 1; PX 1418 at 1).

P14. Topper's capitalization also showed substantial improvement and stability, with two successful offerings of common stock in little more than a year. The price range of its stock had increased from a low of $3 a share in the third quarter of 1970 (PX 462, Exh. 1 at 5) to approximately $15 a share prior to the Private Placement (PX 1370 at 1).

P15. Topper's capital position was strengthened further by a $7 million term loan from the Ford Motor Credit Company (PX 462 at 5) which closed prior to the Private Placement. The Private Placement, plaintiffs were told, would provide further financial stability by lessening dependence on a secured bank loan and reducing the effective cost of interest to Topper (PX 1423 at 9). Thus the Private Placement Memorandum stated:

> "The Company proposes to use the net proceeds of this placement to reduce its bank indebtedness, which

will enable the Company to reduce the effective interest cost on its bank loans. Peak borrowing periods normally occur during the final quarter of the calendar year to finance inventory and receivables during the holiday season and are normally paid back during the early part of the next year" (PX 462 at 5).

P16. The Private Placement was thus portrayed as one further step taken by Topper as part of an overall financial plan to lessen dependence upon a secured financing arrangement under which substantially all of its assets were pledged to secure advances on a demand basis (PX 462, Exh. 1 at 12). Along these lines, the Private Placement Memorandum stated that secured bank loans of $19.6 million on March 31, 1971 would be reduced to $3 million after the Private Placement (PX 462 at 5), and eventually would be reduced to the point where Topper's financing was fully unsecured (see PX 1378 at 2; PX 1423 at 9; *Hieronymus Tr.* 585-86, 608). Reflecting this development, the Private Placement Memorandum showed the capitalization of Topper on March 31, 1971 and its adjusted capitalization after giving effect to recent and proposed financings as follows (PX 462 at 5):

Type of Security	*March 31, 1971*	*September 30, 1971*
Secured Bank Loans	$ 19,565,948	$ 3,064,086
Subordinated Notes	5,200,000	3,850,000
Installment Notes	93,955	93,955
Ford Motor Loan	—0—	7,000,000
Private Placement	—0—	5,000,000
Total Debt	$ 24,859,903	$ 19,008,041
Preferred Stock	19,800 shares	19,800 shares
Common Stock	3,030,874 shares	3,689,399 shares

P17. In terms of Topper's current financial position, the Pension Fund and Connecticut Mutual were told that Topper's product lines had received an "excellent reception" in the first part of the year and were now selling on a year round basis (PX 462 at 6). In addition plaintiffs were advised that Topper maintained a system of financial controls which enabled it to coordinate shipments with demand and thus control inventory for both itself and its customers; in addition these reports permitted Topper to age its accounts receivable and thus insure prompt collection of all open invoices (*Thompson Tr.* 395-97, 418, 452; *Mole Tr.* 673-74; *Hieronymus Tr.* 593; PX 1370 at 2; PX 1372 at 2; PX 1378 at 2; PX 1417 at 3; PX 1459).

P18. Plaintiffs were also told by Topper management that it had a close working relationship with Citibank, which received the voluminous financial reports prepared by Topper on a daily and monthly basis, including particularly reports relating to collections and receivables (*Thompson Tr.* 396; see PX 1459). Both plaintiffs were told by Topper management that they were free to speak to Citibank "to get information about Topper's financial condition" (*Thompson Tr.* 399; see *Hieronymus Tr.* 585).

P19. Because it had not independently verified "'the company's current financial condition'" (*Thompson Tr.* 427; see *id.* at 423-24), the Pension Fund, which also enjoyed an investment advisory agreement with Citibank, decided such an inquiry to Citibank was appropriate. Accordingly, on August 25, 1971, a representative of the Pension Fund telephoned the liaison officer between Citibank and the Pension Fund.

P20. In response, the senior Citibank officer responsible for the Topper account called the Pension Fund on

August 27, 1971 and gave a favorable report on Topper's current financial condition.[12] Among other things, Citibank represented to the Pension Fund that Topper had performed well in a Citibank audit of its receivables, that Topper's principal product line was faring well at retail, that there were no current problems with the Topper account and that Citibank anticipated none.

P21. The fact of Citibank's favorable report on Topper's financial condition was conveyed shortly thereafter to Connecticut Mutual. Thus sometime during the first three days of the week beginning August 30, 1971, Mr. Inglis of CBWL-Hayden, Stone Inc. ("Hayden Stone") telephoned Mr. Hieronymus of Connecticut Mutual to advise, among other things, "that Henry Thompson of U.S. Steel had indeed checked with First National City Bank and had obtained a favorable check on the management of [Topper] and also as to the present financial condition of the Company" (*Hieronymus Tr.* 608-09, 611; see *Thompson Tr.* 449).

P22. Both the Pension Fund and Connecticut Mutual in fact relied on Citibank's favorable report on Topper's current financial condition in connection with their decision to participate in the Private Placement. For its part, Connecticut Mutual discussed this favorable report internally just prior to its decision to purchase $1 million of the Topper securities (*Hieronymus Tr.* 611-12) and was "satisfied" that this report along with other information justified their participation in the Private Placement (*id.* at 612).

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[12] See Plaintiffs' Findings P320 - P321, *infra* at A185-A186.

(ii) *Topper's Successful Product Line*

P23. According to the April 29, 1971 prospectus, Topper manufactured a wide range of toy products, which had been recently augmented by the right to make and distribute a line of educational playthings under the Sesame Street name:

> "The Company manufactures and markets toys for boys and girls. Its products include the *Dawn* line of fashion dolls, clothing outfits and accessories, toy household appliances sold under the name *Suzy Homemaker*, *Johnny Lightning* diecast miniature cars and racing sets, *Ding-A-Ling* robots, *Zoomer Boomer* steel trucks, and dolls, including, among others, *Smartypants*. The Company has recently entered into a royalty agreement pursuant to which it will undertake the design, development, manufacture and distribution, under the 'Sesame Street' name, of a line of educational playthings" (PX 462, Exh. 1 at 3).

P24. Topper's principal toy line was a small fashion doll, with clothing and accessories, introduced under the Dawn name in 1970. According to the April 29, 1971 prospectus, "*Dawn* is a relatively low-priced line of merchandise which is designed to strengthen the Company's goal to minimize heavy seasonal fluctuations through emphasis on toys which sell on a year-round basis" (*id.* at 11; see PX 1370 at 1; *Thompson Tr.* 390-91).

P25. The April 29, 1971 prospectus stated that "December 1970 sales included approximately $14,000,000 of shipments, which consisted primarily of spring program merchandise, carrying extended terms of five to eight months" (the "Spring 1971 Program") (PX 462, Exh. 1 at 8). According to the Private Placement Memorandum, approximately $11 million of these December 1970 shipments were comprised of Dawn dolls and accessories (PX 462 at 6).

P26. The Private Placement Memorandum further stated that such shipments of low-priced merchandise had, by July 1971, in fact proved successful and should accordingly serve to reduce the seasonal nature of Topper's business:

> "The excellent reception to the Spring program and first quarter results indicate that Dawn, as well as the Company's other low-priced products, appears to be selling on a year-round basis and should serve to reduce the Company's seasonal volume and earnings fluctuations" (PX 462 at 6).

P27. During the course of their investigation which preceded the Private Placement, representatives of the Pension Fund and Connecticut Mutual were repeatedly assured that the Spring 1971 Program had been, as the Private Placement Memorandum indicated, successful at retail, and that customers were requesting further shipments of this toy line. Thus:

(a) following his review of the Private Placement Memorandum and the prospectus, Mr. Thompson of the Pension Fund was orally assured by Hayden Stone that Topper's Spring 1971 Program "was a highly successful program, that Hayden Stone had looked into it . . . [t]he merchandise was moving" (*Thompson Dep.* 105); everyone was "sure that [those] goods that were shipped were actually sold" (*id.* at 102-03)—"[s]old by the customers of Topper" (*id.* at 104);

(b) at an August 4 meeting, Orenstein told Thompson "that the Dawn line was doing well and the company . . . actually was re-ordering additional merchandise to replace the Dawn products that had gone into the hands of children" (*Thompson Tr.* 394; see *id.* at 416-18);

(d) likewise, a toy buyer with Zayre Department Stores, a major Topper customer, confirmed to the Pension Fund that "the company has done a good job on *Dawn*" (PX 1375; see *Thompson Tr.* 411);

(e) for its part, Connecticut Mutual was specifically assured by Topper management that the $14 million in Spring 1971 Program receivables, $11 million of which were comprised of Dawn dolls, had been "substantially collected" and Topper was " 'not having or experiencing any delinquencies on this' " merchandise (*Hieronymus Tr.* 591-92); and

(f) these reports of Dawn's success were also repeated to Connecticut Mutual by another large Topper customer, E. J. Korvette, which "indicated that 1971 was not a good year for toys but in spite of this, the Dawn line of dolls was doing pretty well" (PX 1422).

P28. While Dawn and other toys of Topper's current line provided a secure base for Topper's business, the Sesame Street line, which Topper was planning to begin selling by year end, promised to provide even more stability (*Thompson Tr.* 391). Thus the Private Placement Memorandum noted:

> "In March 1971, Topper was awarded a contract to design, manufacture and market a line of educational playthings under the Sesame Street name. This con-

tract was won in competition with the leading toy companies in the United States including Mattel, Ideal and Hasbro. . . . The Company plans to show the Sesame Street line to buyers in 12 major cities throughout the country from late July to mid-August and to accept orders for shipments beginning in October 1971.

"Sesame Street is an extremely well-known children's educational television program which is currently seen by an estimated 8 million children per day. The use of the Sesame Street name represents a unique opportunity for the Company to enter the pre-school educational toy market. Children's Television Workshop's objective is to provide multimedia educational content to the world market through the use of its name. . . .

"In brief, the Sesame Street contract provides that the Company may market all approved toys under the Sesame Street name. The Company provides design and development cost, tooling and advertising. Profits, if any, will be divided equally" (PX 462 at 8-9).

P29. The enthusiastic report on the Sesame Street development in the Private Placement Memorandum was confirmed by Topper customers, as well as by the management of the Children's Television Workshop, which awarded Topper the Sesame Street rights. Thus the toy buyer for J. C. Penney stores told the Pension Fund that he "believes, like everyone else, that *Sesame Street* is a very hot product which will provide some stability in the Topper picture for the next few years" (PX 1376). In a similar vein, an officer of Children's Television Workshop "said that he is 'thrilled' with the job that Topper has done on the *Sesame Street* toys" (PX 1374).

(iii) *Plaintiffs' View of Topper's Business Practices*

P30. The April 29, 1971 prospectus indicated that, to a significant extent, Topper's financial difficulties in 1965 and 1966 were a result of the fact that "customers returned approximately $4,200,000 of toys sold to them under 'bill and hold' arrangements in 1965 and allowances were made to customers of $900,000 against sales made in 1965" (PX 462, Exh. 1 at 8).

P31. While the question of these practices appeared academic in light of the present success which Topper products were currently enjoying, both the Pension Fund and Connecticut Mutual were specifically assured by Topper management, its investment bankers, and at least one outside director, that these prior practices had long since been discontinued.[13]

P32. Thus the Pension Fund was told on August 4, 1971 that Topper was "very hard-nosed about returns" (*Thompson Tr.* 396), that Topper's uncollectible accounts would not exceed $200,000 in 1971 and would probably range about $150,000 (*id.* at 398; PX 1378 at 2), and that in any event Topper would not permit customers to return merchandise which they had failed to sell at retail:

> "[Mr. Thompson]: I phrased my question really to [Mr. Rose] as a general question about sales being final, and then what the return policy was, and he said they were hardnosed and discouraged them. Then I followed up and said, 'Don't you ever do it basically?' And he said, 'Well, sometimes we will balance one good

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[13] *Thompson Tr.* 394-98, 415; *Hieronymus Tr.* 583-85; PX 1377.

selling toy with another.' And then I said, 'Well, what about one that is not selling well?' and he said, 'Well, we definitely don't take back the ones that are not selling and we discourage this'" (*Thompson Tr.* 397-98).

P33. This report was confirmed by an outside director of Topper, Mr. Glover Johnson, a partner in the law firm of White & Case, who told the Pension Fund that Topper's prior "practice of selling on consignment had ended" (*Thompson Tr.* 415). Thus Glover Johnson told the Pension Fund:

> "that Henry Orenstein wanted that consignment selling, as we referred to, stopped, and he said that this was the reason that Orenstein had wanted to buy back Topper from Philadelphia & Reading.
>
> "He . . . said that Orenstein felt that he either had to leave this Philadelphia & Reading organization and found another toy company or else arrange to buy-back here and Mr. Johnson felt that the more honorable thing was for Orenstein to buy-back the company and he cited—he definitely said the practice of selling on consignment had ended and this was the principal reason he gave for Topper coming out of Philadelphia & Reading" (*id.*).

P34. Like the Pension Fund, Connecticut Mutual was also assured by Topper management that the prior bill-and-hold and return practices had been discontinued. Thus, Topper's President, Mr. Orenstein, told Connecticut Mutual that "[d]ue to the fact that he had had a very bad experience with the former policy, this bill and hold, he said that all sales from now on were on a final basis and he never wanted again to get into the situation that he had experienced before" (*Hieronymus Tr.* 584-85).

P35. Orenstein made clear to Connecticut Mutual that it was the prior practice of selling on consignment to supermarkets that was responsible for Topper's prior losses in the mid-1960's. With regard to that prior experience:

> "Mr. Orenstein said that originally he was in the jobber business, selling toys to supermarkets. Wanting to expand into manufacturing, he needed additional capital and sold out to Philadelphia & Reading in order to gain this additional capital.
>
> "After several years the toy market changed, the discount stores started advertising toys as loss leaders, and the supermarket business no longer was viable.
>
> "At this time the president of Philadelphia & Reading became disenchanted with the toy business; he wanted to get out of it. And Mr. Orenstein and a group of investors put some money together, along with a major bank, and bought out the business from Philadelphia & Reading.
>
> "At this time the company was experiencing severe losses because of a lot of inventory piling up. One of the reasons that Mr. Orenstein stated was because it was a bill and hold policy that he had instituted and that during a bad period like this the situation worsens and aggravates itself because the material that you originally thought was sales come[s] back to you and is now back in inventory, which you would have to liquidate" (*id.* at 583-84).

P36. To emphasize that Topper was now selling on a final sale basis, Topper's Senior Vice President—Finance, Mr. Rose, told Connecticut Mutual that if Topper went "out of business" today "[it] would legally be able to collect all these receivables" (*id.* at 592).

P37. Both Topper's independent public accountants, Arthur Young, as well as its investment bankers, Hayden Stone, were equally adamant that Topper had abandoned its prior consignment practices and now sold merchandise on a final sale basis:

(a) Arthur Young's view was most clearly reflected by its certification of Topper's prior financial statements, which provided no indication that reported sales were on anything but a final basis,[14] and stated that Topper's receivables were net only of $569,556 allowance for bad debts (PX 462, Exh. 1 at 30; cf. PX 1378 at 2); and

(b) Hayden Stone representatives repeatedly took the position that Topper had discontinued its prior practices and was now selling on a final basis (*Inglis SEC Tr.* at 112-13).

P38. Appearing to confirm that Topper's sales were final, and that returns were limited to relatively minor amounts of defective merchandise, was Topper's June 30, 1971 unaudited financial statements, which listed only one reserve for doubtful accounts of $569,556 (PX 2 at 2), and an adjustment for returns on only $500,000 (*id.* at 27).

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[14] See Plaintiffs' Finding P156, *infra* at A118.

C.

Plaintiffs' Decision to Participate in the Private Placement

P39. Information distributed and otherwise represented to plaintiffs in connection with the Private Placement portrayed Topper as a financially stable toy company with a record in recent years of steadily increasing sales and profits,[15] whose capitalization had been substantially improved and was therefore significantly less dependent upon secured bank financing,[16] had overcome prior difficulties by discontinuing its consignment practices,[17] was marketing one of the most successful toy items in the country on a year-round basis,[18] and was about to capitalize on a highly favorable long-term contract for the manufacture and sale of a Sesame Street line of toys.[19]

P41. For its part, the Dallas Bank received and reviewed the Private Placement Memorandum as well as the April 29, 1971 prospectus (*Jaynes Dep.* 14). Although the Dallas Bank initially did not believe it wanted to participate in the Private Placement on behalf of the Trust (*id.*), it was persuaded to do so, among other reasons, "because U. S. Steel was going in" and since "U. S. Steel was going in it was a safe investment for" the Trust (*id.* at 33). According to its President, the Dallas Bank agreed to participate because a favorable "recommendation had been made to us by Bernstein-Macaulay" (*Gray Dep.* 35), the investment advisor to the Trust, and because a "substantial portion of the debentures were going to be purchased by the U. S. Steel Pension Fund . . . and . . . some insurance company on the East Coast" (*id.* at 35-36).

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[15] See Plaintiffs' Findings P8 - P13, *supra* at A48-A51.

[16] See Plaintiffs' Findings P14 - P16, *supra* at A51-A52.

[17] See Plaintiffs' Findings P30 - P37, *supra* at A59-A62.

[18] See Plaintiffs' Findings P23 - P27, *supra* at A55-A57.

[19] See Plaintiffs' Findings P28 - P29, *supra* at A57-A58.

II.

TOPPER CORPORATION

A.

Business and Early History

P42. Reportedly one of the five largest domestic toy companies by 1971 (PX 462 at 14), Topper[20] was the successor to a business which commenced the distribution of toys in 1953 (CB ADM 12) under the auspices of Henry Orenstein and his uncle, Marrius Orenstein, who began selling toys to supermarkets on a guaranted sale basis (*Orenstein Dep.* 6).

P43. According to Orenstein, since "these customers in most cases never sold toys before, we had a complete guaranteed sale basis for them" (*id.* at 9): the "customers had a complete right to return the merchandise for a cash refund" (*id.*). This "new approach" proved to be quite profitable for both the customers and the Orensteins (*id. at* 7), and the "business increased to approximately ten million dollars or more" (*id.*).

P44. De Luxe Reading Corporation acquired the business from the Orensteins in 1960 and, in 1964, began eliminating its supermarket business and marketing its products through conventional toy outlets (CB ADM 13 & 14).[21]

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[20] The Company was incorporated in Delaware as De Luxe Topper Corporation in 1966. In 1968 its name was changed to Topper Corporation (PX 462, Exh. 1 at 3). Unless the context otherwise requires, the term "Topper" as used herein refers to Topper Corporation, its business subsidiaries and, where applicable, its business predecessor.

P45. However, De Luxe Reading's parent, Philadelphia and Reading, "had no desire to be just one of several companies" doing business in "the conventional toy market" (*Orenstein Dep.* 15) and "became disenchanted with the business because the business was losing money or was about to lose money" (*id.* at 13).[22]

P46. In October 1966, toward the end of this period of transition from supermarket to conventional outlets, Orenstein, who was the President of De Luxe Reading Corporation under Philadelphia and Reading Corporation's ownership, joined with Marrius Orenstein and a group of 10 other investors to repurchase the business from Philadelphia and Reading Corporation (PX 462, Exh. 1 at 10; CB ADM 15).

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[21] According to Mr. Orenstein, "the sale . . . to Philadelphia Reading" came "about" because "[w]e felt that in order to continue our growth, we needed some capital and we contacted some people who were in this money business and they got us in touch with several prospective investors, and we picked Philadelphia & Reading even though we had offers from others" (*Orenstein Dep.* 10).

[22] Actually, the business "suffered a net loss of $8,622,000 during the first nine months of 1966" (PX 462, Exh. 1 at 3).

B.

Citibank Acts As Commercial Banker

P47. On October 4, 1966 Citibank and Manufacturers Hanover Trust Company ("Manufacturers") advanced $20 million to Topper under an Agreement, as amended from time to time (the "Finance Agreement"), so that Orenstein and his fellow investors could purchase De Luxe Reading from Philadelphia and Reading (CB ADM 17 & 18; *Orenstein Dep.* 20-21; PX 506).

P48. Citibank and Topper remained parties to the Finance Agreement from October 4, 1966 until at least through the end of 1971. Pursuant to its terms, Citibank advanced monies to Topper during this period and has acted as agent for other lenders that, together with Citibank (the "Banks"), at various times also advanced monies to Topper (CB ADM 17).

P49. Under the Finance Agreement, Topper granted the Banks continuing security interest in all accounts receivable, furnished goods and other inventory, machinery and equipment and all "sums at any time standing to the credit of Topper on the books of the Banks" or either of them (PX 506 at ¶ 1; CB ADM 19).

P50. In return, the Banks agreed to lend Topper up to 80% of the face amount of receivables which Citibank, "at their discretion," deemed "eligible" for advances less such reserves as Citibank deemed "proper and necessary". In addition, Citibank, again at its discretion, agreed to lend lesser percentages against Topper inventory valued at the lower of cost or market (PX 506 at ¶ 7).

P51. Under the Finance Agreement, the other participating banks appointed Citibank their agent to make all advances, to accept all assignments, to receive all collections, and to manage the conduct of the loan generally between the banks and Topper (PX 506 at ¶ 11; CB ADM 24).[23] In a similar fashion, Topper was authorized to deal with Citibank "with the same force and effect as if" Citibank was "the sole lender" (*id.*).

P52. Services rendered by Citibank under this arrangement included, among other things, monitoring customer collections and credits on a daily basis and aging Topper's receivables on a monthly basis; as one senior official testified:

> "[A] lending arrangement like this involves a continuing program of assigning accounts receivables as they are created day to day and a continuous accounting for the collections under these accounts receivable.
>
> "This involves a lot of documentation and paperwork, the servicing of which Citibank handled, setting up the controls, setting up the past dues, doing a certain amount of verifications, doing the audits, computing the eligibles and the availability under the lending arrangement, providing an account manager to service the account, that sort of thing.

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[23] In connection with the Finance Agreement, Citibank and Manufacturers executed a contemporaneous and related agreement which specified, among other things, that each "of us shall have a 50% participation in said financing agreement and all transactions thereunder" (PX 507 at ¶ 1); Citibank "shall manage the account under the financing agreement and the transactions thereunder in" its "name" and "will service and manage said account and the collateral in the ordinary course of business and in accordance with [its] usual practice" (PX 507 at ¶ 6).

> "There are a number of things, but it is that sort of thing for all of which we used Citibank people and we were compensated for that" (*Holzman Dep.* 20-21).

P53. For managing the Topper account, Citibank retained as compensation the balance of income received from the Topper loan which was not remitted to other participants (CB ADM 26). For example, in 1971 Citibank charged Topper interest at an annual rate of 9%, but paid Manufacturers Hanover at a rate of 7.18% and Fidelity Union at 6.40% (CB ADM 27; PX 742). As a result of this arrangement, the yield to Citibank from its investment was considerably in excess of the interest rate charged Topper (CB ADM 29).[24]

P54. As of September 17, 1971, Citibank had a 42 percent share of the total loan outstanding to Topper under the Finance Agreement, excluding the Ford Motor loan of $7 million.[25] Manufacturers Hanover had a 43 percent participation and Fidelity Union Trust Company had a 15 percent participation (*Citibank Interr. Resp. II* at 5).

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[24] "The 'yield' to Citibank from the Topper loan . . . is calculated by dividing the total compensation retained by Citibank applicable to any specified period of time by the actual average outstanding principal balance of Citibank's share of the Topper loan during the same period" (*Response of Defendant First National City Bank to Second Set of Interrogatories of Plaintiffs,* dated January 15, 1975 [*Citibank Interr. Resp. II*], at 9). Thus, in 1967, Citibank had a "yield in excess of 13%" based on an interest rate of 9.47% (*id.* at 5; PX 741 at 2).

[25] As of September 17, 1971, the total secured loan to Topper was $20,147,404, including the Ford Motor loan of $7 million. Ford Motor's share of the total loan was 35%; Manufacturers Hanover's share was 28%; Citibank's share was 27%; and Fidelity Union Trust Company's share was 10% (CB ADM 23).

P55. At the time of the Private Placement, the "Topper account in total dollars was the largest account" under the supervision of the Citibank Factoring and Commercial Finance Division (*Siegel Tr.* 1125; CB ADM 22) with "substantially" greater sums than the other accounts (*Waldman SEC Tr.*[26] 9-10).

P56. The total amount of compensation received by the Banks from Topper under the Finance Agreement compared with the amount of compensation retained by Citibank for its own account as follows (CB ADM 30):

Year	*Total Compensation*	*Citibank Compensation*	*Citibank Share as Percent of Total*
1969	$1,443,589	$547,666	47.9%
1970	$1,549,572	$732,703	47.3%
1971	$1,351,827	$702,815	50.5%

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[26] Transcript of Testimony by Edward Waldman Before the Securities and Exchange Commission in *In Re Topper Corporation*, File No. 6678, May 30, 1973 ("*Waldman SEC Tr.*").

Findings of Fact

C.

Sales and Marketing Practices of Topper

P57. Although Topper purported to have discontinued its policy of selling merchandise on a consignment or guaranteed sale basis in 1967, as a matter of business practice Topper continued, during the years 1968 through 1971, to grant concessions to major customers who were unable to sell any substantial amount of Topper merchandise at retail.[27] As one major customer testified:

> "As we continued to purchase, and as is the case in the toy industry with several other major manufacturers, when an excess quantity of merchandise was carried over they either helped us out by offering return[s] sometimes, sometimes they even offered a credit against the merchandise to help us sell it, and other times they redated it, depending upon the situation, and it was always negotiable at the top level" (*Sieff Dep.* 10-11).

P58. According to Topper management in 1972, there were two ways to sell merchandise in the toy industry: "1) the customer places the order and he must live and die by his decision 2) if the manufacturer writes the order, they must relieve his year end inventory problems through exchange, return or markdown. Topper sold merchandise in accordance with number two above" (PX 865 at 8).

P59. Arthur Young, too, shared the view that Topper had a "history of making concessions" (*Walsh Dep.* 263-

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[27] See Plaintiffs' Findings P63 - P68, *infra* at A74-A76.

64), generally at Toy Fair in late February, to major customers unable to sell a substantial part of their previously purchased Topper inventory the previous Christmas (CB ADM 103). As Topper's chief executive officer in 1972 explained, Topper employed "a marketing procedure whereby unsold inventory [was] what they euphemistically called adjusted at toy fair every year" (*Clarke Dep.* 64-65). This long-standing Topper practice was described by counsel for one typical Topper customer* as follows:

> "It is our understanding that this merchandise was shipped to our client by your company upon the understanding that it was returnable to you at any time by our client or, in the alternative, mark-downs would be allowed to make the merchandise salable by our client. Such arrangement was the same as many previous arrangements between you, and was in accord with your long-standing course of dealing and usage of trade. These arrangements and practices between our client and you have been affirmed and reaffirmed on so many occasions between your representatives and representatives of our client that it is difficult for us to understand your present conduct" (PX 903 at 2).

P60. Almost all major Topper customers received, or had the right to receive, one or more of the "many different types" of concessions offered by Topper "in the area of mark-downs, rebates, special allowances, exchange privileges, returns" and the like (*Samuels Dep.* 106). The "larger customers all had some type of arrangement, whether it be one type of concession or another" (*id.* at 109-10; *Sieff Dep.* 58-59). These arrangements were particularly evident with large retailers such as Kresge,[28] Korvettes[29] and Times Square Stores,[30] as well as Topper's franchise distributors, as Orenstein explained:

> "The franchise distributors were given substantial privileges. They got an extra discount and, in return, they had to perform certain things for the company which the other customers were not required to perform.
>
> "With these distributors we went further as far as cooperating with them because of the obligation that they had undertook with us than with other customers. For example, if they had to carry an item in the line and if at the end of the year, or Toy Fair, they had inventory, and if they needed some exchanges or if they needed some advertising allowances over and above what we originally granted, we would, depending upon each situation, give it to them, subject to our continuing relationship, and very often subject to new orders" (*Orenstein Dep.* 256-57).

P61. Granting concessions to major customers was integral to Topper's business, for if Topper failed to accommodate overstocked customers, it ran the risk of losing their future business (CB ADM 109).[31] An example of the risks inherent in refusing to grant customers one type of concession or another occurred in 1968 or 1969 when Topper refused to issue credit for merchandise returned by one major entity, Sears Roebuck & Company. As a result,

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[28] See PX 836, 833, 834, 966.

[29] See PX 799, 800, 801, 845.

[30] See PX 851, 845, 806, 946.

[31] See *Rose Dep.* 199-200; PX 857, 875, 851, 909, 917, 1257, 808, 809A, 915.

Topper lost Sears Roebuck & Company business for a period following that refusal (CB ADM 109).

P62. In this light, Topper as a matter of business course solicited toy orders from customers with the understanding that it would "work with" or "protect" the customer in the event the goods were not sold—i.e., determine the type of concession most appropriate under the circumstances, either returns, exchanges, markdown allowances, rebates or the like (CB ADM 110 and 111).[32]

P63. Most prominent of the concessions Topper granted customers was permitting the return of non-defective unsold merchandise directly to its Elizabeth, New Jersey plant (CB ADM 104).[33]

P64. Another form of concession granted by Topper to its customers was undertaking to "move", "tranship", or "reship" unsold merchandise from one customer to another in lieu of the customer's returning the merchandise directly to Topper's plant in Elizabeth, New Jersey.[34]

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[32] *Greenman Tr.* 299, 320-21; *Ades Tr.* 212-13; ***Monchik Tr.*** 181-82; PX 1117, 842, 837, 836, 896, 1350, 846, 1194, 849, 895, 888, 891, 881, 897, 883, 876, 1353, 885, 890, 878, 847, 887, 873, 1354, 841, 886, 892, 874, 840, 1352, 893, 838, 1355, 1195, 1196, 1360, 889, 1452, 875, 850, 798, 884, 799, 800, 801, 802A, 901, 843, 802, 1362, 1324, 899, 905, 844, 906, 845, 907, 909, 908, 1333, 917, 806, 1091, 915, 1112.

[33] See, *Pierce Dep.* 177-78; *Sieff Dep.* 13-16; ***Monchik Tr.*** at 182-90; *Greenman Tr.* 297-98, 313; *Ades Tr.* 207-08; PX 752, 837, 1249, 1343, 1250, 1252, 1253, 753, 756, 1202, 1344, 1345, 1317, 1319, 881, 887, 874, 893, 1198, 1320, 839, 1321, 1326, 1327, 1328, 1329, 1330, 1331, 1332, 1204, 910, 805, 905, 1223, 904, 851, 909, 1197, 1257, 915, 916, 882, 1112, 903, 1454.

[34] See *Pierce Dep.* 412-14; *Sieff Dep.* 30-34; ***Greenman Tr.*** 315-16; *Ades Tr.* 212; PX 757, 888, 891, 889, 1452, 1200, 1323, 901, 899, 907, 908, 1257.

Findings of Fact

P65. Related to the practice of permitting returns was Topper's "exchange" policy pursuant to which Topper permitted customers to exchange one type of unsold merchandise for another or for credit against any future order of merchandise (CB ADM 122, 123, 125-133 and 136).[35]

P66. In practice, the right of Topper customers to exchange one line of merchandise for another differed little, if at all, from the practice of permitting returns (*Pierce Dep.* 353, 360)—*i.e.*, both involved the return shipment of merchandise and the issue of credit, and both were predicated upon the prospect of some future business dealing between the parties (*Greenman Tr.* 293). Orenstein himself equated the term "exchange" to mean "subject to protection" (*Orenstein Dep.* 78-79) as did Topper's Vice President-Sales (*Pierce Dep.* 112-13) who also equated the practice with a "guaranteed sale" (*id.* at 95-97; PX 909).

P67. In other instances, Topper, again in lieu of permitting returns or arranging for transshipments between customers, granted credits to customers in the form of markdowns, rebates, price adjustments and "advertising allowances,"[36] to enable them to sell their Topper inventory at reduced prices without suffering any financial loss themselves (CB ADM 105).[37]

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[35] See *Pierce Dep.* 150-51, 157-59, 14-21; PX 835, 1184, 1342, 837, 834, 900, 754, 755, 1351, 849, 895, 888, 891, 881, 897, 876, 883, 1353, 885, 890, 878, 898, 847, 887, 873, 1354, 833, 886, 892, 874, 840, 1352, 893, 838, 1359, 884, 799, 502, 844, 907, 908, 1333, 896, 1193, 894, 1260, 901, 904, 910, 1100A.

[36] According to Arthur Young, "advertising allowances" were "a euphemism for additional discount" (PX 919 at 3) which were "granted to customers having problems moving certain items" (PX 1023 at 2)—"[o]nly rarely is proof required of actual advertising. In most cases, there is no reason to believe that this credit is being used for advertising" (*id.* at 2). And Topper customers agreed (see, *e.g.*, *Ades Tr.* 212-13), as did Topper's Vice President-Sales (*Pierce Dep.* 137-38).

P68. Another form of concession which Topper granted customers was redating or extending the due date of receivables when the underlying merchandise had not yet been sold (CB ADM 180, 184, 185 and 187).[38] The purpose of redating was to induce customers who were unable to sell merchandise during a particular season, generally Christmas, to retain the merchandise and attempt to sell it at a late date (CB ADM 181); however, Topper, not its customers, was responsible for redated inventory.[39]

P69. Even with these concessions, Topper customers were not always willing to accept shipments of Topper merchandise. Over the years Topper, in these instances, made various arrangements with customers to warehouse merchandise on or near its Elizabeth, New Jersey premises until such time as the customers elected to request shipment of the goods (CB ADM 32, 140-53, 155-59, 161-72 and 174). Topper, however, reported the warehouse transactions as sales when the goods were placed in the warehouse (*Cook Dep.* 25), not when (or if) they were ever shipped to customers.

P70. Topper's initial experience with warehousing in 1965 proved quite disastrous, as customers "returned" approximately $4.2 million of the $7 million in merchandise stored in a Topper warehouse under "bill and hold" arrangements (PX 1367).

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[37] See *Pierce Dep.* 135-38; *Sieff Dep.* 34-35, 39-40; *Greenman Tr.* 295, 302; *Ades Tr.* 206, 212-13; PX 1025, 919, 842, 1249, 1343, 1255, 1256, 1318, 1254, 889, 1452, 1023, 1025, 1349, 1201, 911, 804, 899, 904, 907, 809A, 915, 1115, 1112, 903.

[38] See *Pierce Dep.* at 153; PX 922, 464, 1342, 837, 1450, 1451, 1344, 1194, 876, 885, 890, 878, 887, 874, 840, 893, 838, 912, 719, 720, 721, 722, 723, 724, 725, 726, 727, 728, 729, 730, 731, 732, 733, 734, 735, 736, 1322, 877, 879, 914, 901, 911.

[39] See, *e.g.*, *Greenman Tr.* 313-15; *Ades Tr.* 214; PX 858, 1343, 1452, 1346, 1321.

P71. Despite this experience, Topper again began storing merchandise on its premises as early as 1967, this time under the auspices of the New York Terminal Warehouse Company, an independent public warehouseman (CB ADM 140 and 141; PX 1171). Under the warehouse program, Topper leased space to the warehouseman for $1 a year (PX 921 at 4) staffed the warehouse with its own employees (*id.* at 2), agreed to pay all warehouse costs for the customers (PX 470-492), insured the merchandise at its own expense (*id.*), had the right to remove merchandise from the terminal warehouse without prior notice to the customers (PX 493-96; 981-92), and permitted customers to substitute a different item from that originally reported as "sold" and stored in the warehouse (CB ADM 161).

P72. The apparent similarity between the New York Terminal Warehouse program and the bill and hold program undertaken in 1965 was confirmed in early 1970, when Topper permitted Kresge to return at least 50% of the $400,000 in merchandise billed to Kresge at the end of 1969 and held for its account in the New York Terminal Warehouse (CB ADM 145 and 146); Orenstein himself claimed that it was $500,000 out of a $1.2 million warehouse order which he permitted Kresge to return in 1970 (PX 836 at 1).[40]

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[40] According to Arthur Young these returns represented "a marketing decision made in 1970, because Kresge basically didn't want the merchandise. And they made it in order to induce, or keep Kresge, their largest customer, on good terms" (*Cook Dep.* 54-56).

P73. The warehouse program was substantially expanded at the end of 1970 to encourage year-end purchases from Topper customers who were otherwise unwilling to accept goods past the Christmas season. As of December 31, 1970, $7 million of merchandise was either stored in or in transit to the New York Terminal or other warehouses from the Orient (CB ADM 151).

P74. Between January 1, 1971 and August 31, 1971, Topper had transferred an additional $5.6 million to the New York Terminal and Woodbridge warehouses located at or near its Elizabeth, New Jersey plant (PX 1001), in addition to the $7 million warehoused in December 1970 (CB ADM 172).

P75. In other instances in 1971, Topper shipped merchandise to outside warehouses,[41] and recorded the transaction as a sale, when the customer had no intention of selling the merchandise itself (CB ADM 169; *Samuels Dep.* 78-80; see PX 1198, 1199, 1200). As management observed in 1972:

> "Topper had entered into a warehouse arrangement with several customers, including Lionel Leisure and Blatt Distributing. Under this agreement, Topper shipped and billed approximately $1,000,000 to Lionel Leisure's warehouses in Georgia and Florida.
>
> "However, these shipments did not represent outright sales. Lionel would only warehouse the merchandise and redistribute to the ultimate purchaser

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[41] The total amount of merchandise warehoused by Topper at these outside locations is unknown. However, subsequent management found there was a substantial amount of inventory all over the country in outside warehouses (PX 1117 at 4).

> at Topper's direction. This enabled Topper to facilitate delivery to distant customers during the anticipated peak season. In consideration, Lionel would earn a 9% warehousing fee in the following manner: originally billed at an effective rate of 81% list, they received credit upon shipment at 90%. Even more important was the fact that Topper's customers purchased only $80,000. The agreement with Lionel itself resulted in a considerable overstatement of profit at September 30, not to mention the other five major customers who were involved" (PX 1117 at 4).

P76. Even with the New York Terminal merchandise, however, customers had no obligation to accept shipment. Thus Topper agreed with at least 23 major customers that merchandise stored in the New York Terminal Warehouse was to be paid for only as those customers withdrew the merchandise from the warehouse, or with certain of these customers, if not sold, transferred by Topper to another customer or exchanged for different merchandise (CB ADM 162). This was a concession over and above the various adjustments which Topper made for merchandise which customers failed to sell at retail. Thus one distributor explained that the warehouse "merchandise would remain Topper Corporation's property, but that I would have the right to draw on or acquire all or part of the ordered merchandise if I so desired"; beyond that, merchandise "delivered to The S & M Company would be fully and freely returnable to Topper Corporation for cash or credit" (PX 1258; *Sieff Dep.* 49-56).

D.

Significance of Topper's Concession Policy

(i) *Amount of Credits Critical to Topper's Profitability*

P77. The net effect of the various arrangements between Topper and its customers was that Topper toys were sold on a basis akin to consignment.[42] In this light, the true measure of Topper's success was not the amount of "sales" it was able to report, but whether Topper merchandise was actually sold to the ultimate consumer at retail (*Weiss Tr.* 782-83; *Lusk Tr.* 1100).

P78. Merchandise which had failed to sell at retail was subject to adjustment under Topper's concession policy. With the exception of redating, where customers agreed to retain the merchandise on a strict consignment basis,[43] concessions were granted by issuing credits against customer accounts for merchandise returns or exchanges, or in lieu thereof, for rebates, markdowns, price adjustments, or advertising allowances to enable the customer to sell Topper inventory without loss.

P79. In addition, at the end of each year Topper accrued or reserved for the amount of credits it estimated would be granted customers for returns, discounts, allowances and other concessions above and beyond the amount of credits already granted and recorded during the year (CB ADM 112). According to Arthur Young, there was a "dramatic increase" (PX 1065 at 2) in the amount of such reserves from 1969 to 1970—$4,688,949 in 1969 compared with $8,551,870 in 1970 (PX 1038; CB ADM 113).

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[42] "[T]he presence or lack of an obligation to purchase or pay for the goods is the distinguishing characteristic" between a sale and a consignment. If "the owner of the goods delivers them to another to be sold by him with no obligation to pay for those unsold, the transaction is consigment. . . ." 4A W. Collier, *Bankruptcy*, ¶ 70.18, at 211-13 (14th ed. 1976).

[43] See Plaintiffs' Finding P68, *supra* at A76.

P80. As far as Topper's customers were concerned, the type of concession, be it a return or some form of markdown allowance, mattered little since the effect of each credit issued was to reduce that customer's liability to Topper.[44] Thus one West Coast distributor explained three of the several different ways Topper could issue credits for unsold inventory:

> "It could happen one of three ways. The one that I mentioned to you, where they would negotiate a deal, we might invoice the customer at the new lower price, receive a credit. I believe there were circumstances where they sold the merchandise direct or would invoice the retail customer direct, and then we would receive a credit for the purchase that we had paid; and then a third was that they had a warehouse in Clearfield, Utah, a public warehouse there, and I believe in certain instances we just shipped the merchandise back to Clearfield under their account and we received credit" (*Ades Tr.* 208).

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[44] See, e.g., *Ades Tr.* 207-08; *Greenman Tr.* 293-95; PX 842, 752, 1343, 837, 1249, 1250, 1252, 1253, 753, 756, 1202, 1255, 1256, 1318, 1254, 881, 887, 874, 893, 1198, 839, 889, 1452, 1023, 1025, 919, 1204, 910, 1201, 911, 804, 805, 899, 905, 904, 851, 907, 909, 1197, 1257, 809A, 915, 882, 916, 1115, 1112, 903.

P81. The true success or failure of Topper's product line, therefore, was reflected by the relationship between gross sales, or shipments, on the one hand and the amount of credits issued for various concessions on the other (CB ADM 119; PX 1435; *Schwartz Dep.* 720-21; *Weiss Tr.* 153-56).

P82. For the three-year period 1967 through 1969 the amount of credits which Topper issued customers for various concessions averaged 14.5% of gross sales (PX 1435). Significantly, however, credits increased substantially in 1970, reflecting a marked downturn in the acceptance of Topper's products at retail.[45] Thus the amount of credits issued by Topper for returns, allowances, discounts and other concessions increased from $9 million in 1969 to more than $19 million in 1970 (*id.*), reducing Topper's sales from a "gross" figure of $83.3 million to a "net" figure of $63.9 million. Viewed in light of Topper's operations as a whole, the amount of credits attributable to customer concessions increased from 14.8% of gross sales in 1969 to 23.3% in 1970:

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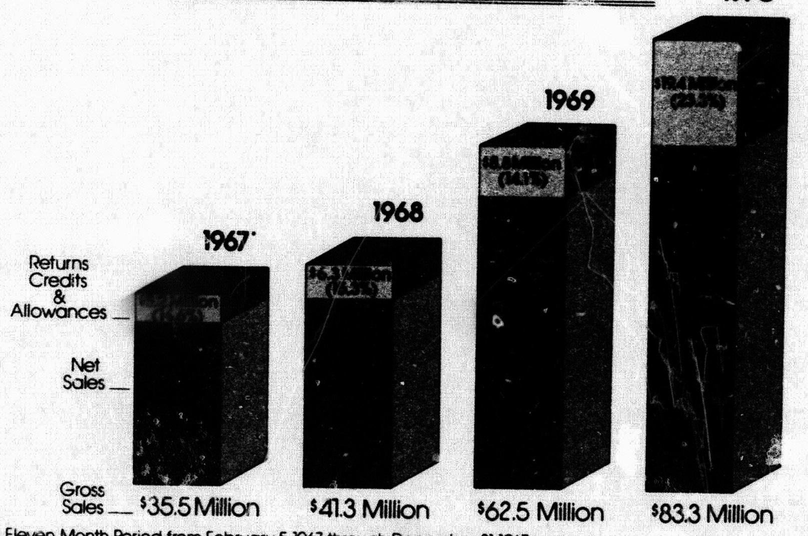
[45] See Plaintiffs' Findings P117 - P123, *infra* at A100-A103.

PX1435

TOPPER CORPORATION

GROSS SALES vs. NET SALES



* Eleven Month Period from February 5, 1967 through December 31, 1967

SOURCE: Topper Corporation Summary of Gross Sales, Discounts & Allowances, Returns, & Net Sales As Listed In Prospectus attached to a letter from Julius H. Schwartz to Mr. Conrad K. Sterrett, dated May 6, 1970 (PX 460; Citibank Admissions 119 & 422) and Sales-Gross Year to Date 12/31/70 (PX 1015; Citibank Admissions 119 & 947) and Topper Corporation Consolidated Statement of Operations included within the Private Placement Memorandum (PX 462; Citibank Admission 428)

(ii) *Failure to Disclose Significance of Concessions Policy to Plaintiffs*

P83. Despite the significance of Topper's concession policy to its business, none of the sales and marketing practices which comprised this policy, individually or as a whole, were disclosed to plaintiffs at any time prior to the Private Placement. Thus under neither the "trend" section of the April 29, 1971 Prospectus (PX 462, Exh. 1 at 8), the "Products" section (*id.* at 10-12), the "Marketing" section (*id.* at 12), the "Recent Developments" section (*id.* at 14), the "Competition" section (*id.* at 15), or in any other part of the Prospectus or in the Private Placement Memorandum did Topper in words or substance disclose:

(a) that as a matter of business practice, toy sales were subject to subsequent adjustments or concessions in the event customers were unable to sell any substantial amount of Topper merchandise;[46]

(b) that such adjustments or concessions were required by the nature of the promotional toy business, and failure to grant such concessions in the future could adversely affect Topper's relationship with major toy distributors;[47]

(c) that sales reported for prior financial periods were net of the amount of credits issued, accrued or reserved for by Topper for returns, rebates, discounts, allowances and other adjustments or concessions, and that the amount of such credits increased from approximately $9 million in 1969 to $19 million in 1970, or as a percent of gross sales, from 14.8% in 1969 to 23.3% in 1970;[48]

(d) that there was no assurance that the amount of credits issued in 1971, or future years, would not materially and adversely affect Topper's profitability for those years;[49] or

(e) that a substantial portion of reported sales involved merchandise stored in a warehouse located on Topper's premises under terms comparable to its prior bill and hold arrangements; that customers were not obligated to accept shipment of merchandise from such warehouse unless and until a retail demand for the product arose; and that Citibank had declared all warehouse transactions subsequent to March 10, 1971 ineligible for advances under the Finance Agreement.[50]

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[46] See Plaintiffs' Findings P62 - P68, *supra* at A74-A76.

[47] See Plaintiffs' Finding P61, *supra* at A73-A74.

[48] See Plaintiffs' Finding P82, *supra* at A82-A83.

[49] See Plaintiffs' Findings P77 - P79, *supra* at A80-A81.

P84. Nor were any of these material practices disclosed, or indeed even hinted at, in Topper's consolidated financial statements or accompanying footnotes. Thus the financial statements simply reported Topper's "net sales" (PX 462, Exh. 1 at 6) without disclosing the amount of gross sales or the relationship between net and gross sales (*Weiss Tr.* 156). In terms of what those sales were "net" of, the accompanying balance sheet indicated that receivables arising from those sales were "less allowance of $569,556 for uncollectable accounts" (PX 462, Exh. 1 at 30) and nothing else.

P85. No mention was made in the financial statements or the April 29, 1971 Registration Statement of any of the $8.4 million reserves for returns and concessions established at the end of 1970[51] (*Weiss Tr.* 780-81), even though Regulation S-X of the Securities and Exchange Commission in effect during 1971 specifically required that Topper "[l]ist, by major classes, all reserves not included in specific schedules" and to "[i]dentify each such class of reserves by descriptive title" 17 C.F.R. § 210.12-13 (1971).

P86. Because there was no indication in either the financial statements or the prospectus concerning the fact of these reserves (*Weiss Tr.* at 780-81), Mr. Weiss of Price Waterhouse concluded there was "nothing in the statements that would lead you to believe that these sales were other than final sales" (*id.* at 785).

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[50] See Plaintiffs' Finding P105, *infra* at A93-A94.

[51] See Plaintiffs Finding P79, *supra* at A80-A81.

P87. In like fashion, there was nothing disclosed in the financials which indicated that Topper permitted customers to return anything but relatively minor amounts of defective merchandise: "Topper's returns . . . would seem to be quite minimal, because the uncollectible accounts is extremely small as compared to receivables. It seems that their collectability history should be very good, in fact, it should be excellent" (*Weiss Tr.* 781).

P88. Moreover the existence of these practices, as well as of their significance to Topper's operations, ran directly contrary to specific representations made during the course of plaintiffs' investigation prior to the Private Placement.[52] For instance, Mr. Thompson of the Pension Fund was told by Mr. Rose that all sales were "final", that Topper was "very hard-nosed about returns" (*Thompson Tr.* 396), and that they "'definitely don't take back the ones that are not selling'" (*id.* at 398). For another example, Mr. Orenstein told Mr. Hieronymus of Connecticut Mutual that "[d]ue to the fact that he had a very bad experience with . . . bill and hold, he said that all sales from now on were on a final basis and he never wanted again to get into the situation that he had experienced before" (*Hieronymus Tr.* 584-85).

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[52] See Plaintiffs' Findings P30 - P38, *supra* at A59-A62.

E.

Citibank Was Fully Aware of Each Significant Sales and Marketing Practice

(i) *Knowledge of Returns and Concessions*

P90. Most basically Citibank was aware that as a matter of business practice Topper granted concessions to major customers who were unable to sell Topper inventory. Indeed the practice of granting concessions was considered one of the "inherent problems" in the toy industry by Citibank's Mr. Siegel:

> "The problems, as I saw it in the toy industry, inherent, is the relationship between manufacturer and the customer . . . particularly with toys . . . concessions have always been made with major customers, based on competition and demand with respect to merchandise sold, and that the retailers, particularly the large retailers, were very much a major force in this sort of understanding that they had with the supplier, and that it promoted instances where suppliers would have to make concessions for various reasons at various times, under many circumstances which would normally not be found in other industries" (*Siegel Dep.* 333-34).

P93. Pursuant to this provision, Topper submitted to Citibank practically each working day a credit schedule "showing the daily total of credits on merchandise returns and other items, attached to which was a computerized credit register itemizing and totalling the credits by customer and, in the case of merchandise returns, showing the number and the description of pieces returned"

(*Citibank Interr. Resp. I*[53] at ¶ 14(a)). The amount of credits reflected on these credit schedules was then totaled on a month-to-date basis by a Citibank computer which prepared daily Advance Sheets for the review and guidance of Citibank officials.[54]

P94. Mr. Siegel of Citibank "pointed out" to an officer from Ford Motor Credit in 1972 that Topper "had an exchange program for some time and that it had been their normal practice to exchange goods wherever possible" (PX 1551 at 4); according to Mr. Lusk, such exchanges were deemed "ineligible" for advances by Citibank (*Lusk Tr.* 1055). In reply to a question, Siegel also indicated in 1972 that "advetising [*sic*] allowances are a gimmick" (PX 1551 at 4-5) and Lusk testified that they were considered part of the overall reserve established by Citibank against Topper's receivables (*Lusk Tr.* at 1055).

P95. Most significantly, Citibank understood the significance of the amount of credits to Topper's toy operations. Credits issued to customers were commonly referred to as "dilution" in Citibank audit reports which periodically commented on their significance to the Citibank officials responsible for the Topper account.[55] Dilution, according to Citibank's Mr. Lusk, was "the difference between what is the amount originally billed and the amount subsequently collected" (*id.* at 1100); or "the percentage of credits and allowances and deductions to gross receivables" (*Siegel Dep.* 497-99).

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[53] *Response of Defendant First National City Bank to Interrogatories of Defendants Hayden Stone Inc., Bernstein-Macaulay, Inc., Roger S. Berlind and Sanford I. Weill,* dated August 12, 1974.

[54] See Plaintiffs' Findings P212 - P213, *infra* at A154-A155.

[55] See PX 700 at 2-3; PX 701 at 3; PX 702 at 3; PX 703 at 2.

P96. Citibank also knew that dilution was the result of "return privileges" (PX 700 at 2) as well as "[d]iscounts of all kinds, advertising, credit discounts, volume discounts" and the like (*Lusk Tr.* 1100-01). Dilution went up at Topper in 1970, Citibank was aware, "mainly because of advertising allowances and more liberal return privileges" (PX 700 at 2). More "liberal return privileges" in the eyes of one Citibank officer meant "having given more return arrangements to a greater number of customers" (*Lusk Tr.* 1111).

(ii) *Citibank Protected Its Collateral From "Dilution" Caused by Concessions*

P97. Citibank took steps to protect its collateral from the "dilution" to sales and receivables caused by Topper's concessions. Thus the Finance Agreement authorized Citibank, at its sole discretion, to deem various receivables ineligible for advances and to create "such reserves as they may deem proper and necessary" (PX 506 at ¶ 7). When asked by Manufacturers Hanover in 1966, "to explain what accounts we will deem ineligible as a matter of general practice", Citibank listed, among other accounts, receivables "unpaid for 60 days past due date" and "[c]onsignment and guaranteed sales" (PX 508).

P98. In accord with this "general practice", Citibank at the end of each year established a reserve for returns and other concessions on its own books, above and beyond the 20% reserve for dilution built into the lending formula (*Lusk Tr.* 1108-09). According to Lusk, "discounts and allowances were treated as part of the dilution in the accounts receivable and provided for in the 20 percent equity that we maintain" (*id.* at 1055).

P99. It was Citibank's practice to "take a very conservative approach to establishing a reserve for returns" (PX 674; *Lusk Tr.* at 1109-10). The effect of such reserve was to reduce the amount of funds available for advances, and thus isolate Citibank from financial perils associated with Topper's concession policy.

P100. Illustrating Citibank's knowledge of redating as well as its significance to Topper's business is the deposition testimony of Mr. Holzman:

> "Redatings, as I understand the term used in that memorandum (PX 712), represented merchandise that was shipped in one season, and which was due and payable according to terms extended in that sale, which probably were not sold by our client's customer during that season, the customer having come back to our client and asked for some relief in his obligation to pay the invoice.
>
> "And in order to keep his customer happy, an agreement was entered into, in which our client extended the dating terms to a new season.
>
> "It was my judgment that that type of account should not be considered as an eligible account receivable entitled to an advance" (*Holzman Dep.* 42-43).

P101. Receivables redated by Topper in 1970 and 1971 were, in significant measure, reserved against or deemed "ineligible" by Citibank for lending purposes under the Finance Agreement, thus:

(a) after Citibank initially learned of redating on or about January 15, 1970 (PX 667 at 2-3), it established a "reserve" of $1.5 million against the total of $2.5 million of redated receivables (CB ADM 188; PX 668; *Waldman Dep.* 92-93; *Lusk Dep.* 39-40); the rationale for this reserve was that if the receivable "was not paid according to original terms . . . it didn't represent an account receivable that had the same integrity as one that did pay according to terms or substantially in accordance with terms, and it was not entitled to the same credit worthiness" (*Holzman Dep.* 43);

(b) further, "[a]ccounts receivable which were redated in early 1971 were considered ineligible (until paid), despite the receipt of confirmations after the 1971 Toy Fair, until on June 7, 1971, Citibank agreed to advance 50% against redated (unpaid) accounts receivable until the end of the month following the extended due date" (*Citibank Interr. Resp. I* at 46; CB ADM 189; PX 689);

(c) however, Citibank only agreed to advance 50% of the face value of redated receivables in June 1971 *after* Topper confirmed that approximately $12 million in outside capital would be forthcoming to reduce Citibank's loan balance from plaintiffs and Ford Motor Credit Company (PX 689 & 541); and

(d) Citibank's conservative posture on redating proved justified when a subsequent study by Mr. Siegel showed that 1971 redatings had not been paid by November 22 of that year (*Siegel Tr.* 1156; PX 703 at 3).

P102. As far as warehousing was concerned, Citibank recognized that despite the public warehouse feature, the program was essentially nothing more than the type of bill and hold arrangement which gave rise to Topper's difficulties in 1965. Thus Citibank referred to the program as "the current 'bill and hold' arrangement at the Elizabeth warehouse" (PX 683) because "it was in effect part of the Topper property" and "not really an independent outside special warehouse located and controlled by others" (*Waldman Dep.* 181). For this reason, Citibank "viewed the terminal warehouse arrangement as meaningless from the point of view of reflecting a sale" and "insuring us that the customer would pay" (*id.* at 144). As one Citibank officer testified,

> " '[n]ow, maybe legally you could transfer ownership on the premises of a seller, but the practicalities of collecting on something like this we found in the past and assumed in the future would be somewhat difficult' " (*Siegel Tr.* 1159).

P103. The warehouse arrangements negotiated by Topper with its customers were responsible for Citibank declaring the receivables related to those transactions "ineligible" under the Finance Agreement (CB ADM 175). Citibank's position was first communicated to Topper by Mr. Joseph Hinsey, outside counsel to Topper, who reported on March 16, 1971 that lawyers for Citibank expressed "[concern] that such a 'bill and hold' arrangement creates a substantial risk of the customer's rejecting the goods upon delivery in the future and thus jeopardizing First National City Bank's position in financing accounts receivable for Topper" (PX 497 at 2).

P104. Topper subsequently prepared a revised warehouse agreement which it submitted to Citibank on May 12, 1971 (PX 498), and which was forwarded in turn to

Citibank's counsel, who advised on May 20, 1971 that "Topper's counterdraft does not protect you; A [*sic*] strong customer can find good reasons for not making payment because the transaction is still incomplete" (PX 500 at 3). According to Citibank's counsel, the warehouse transactions were "incomplete", among other reasons, because:

> (a) "[t]he word 'promotion' carries an overtone of sale and return or of a tentative agreement only" (*id.* at 2);
>
> (b) the "first paragraph of our letter states that Topper has sold certain merchandise . . . [t]his has been changed to state only that Topper will deliver certain merchandise" (*id.*);
>
> (c) because "Topper's draft provides that Topper may *replace* merchandise in the event of damage or loss . . . Topper does not have the right to replace under ordinary commercial arrangements" (*id.* at 3); and
>
> (d) finally "[a]lmost every problem you have had with bill-and-hold merchandise in the last year has arisen out of changes made without the bank's consent. An arrangement under which your client and its customer can change bill-and-hold orders renders a bill-and-hold agreement of only limited utility. You are then dealing with something less than a completed transaction" (*id.*).

P105. Despite this advice, "the warehousing agreement was never revised" (*Waldman Dep.* 141), and Citibank declared that after March 10, 1971 all receivables related to the warehouse program "were deemed ineligible as security for loans to Topper, and Topper was required to separately state the amount of bill and hold sales represented in each daily invoice register and to separately categorize bill and hold accounts receivable on its monthly aging reports" (*Citibank Interr. Resp. I* at 43-44).[56]

P106. Again Citibank's caution on the treatment of warehouse receivables appeared prudent when Topper permitted customers to "return" approximately two-thirds of the merchandise stored in the warehouse on August 31, 1971 (cf. PX 1437; CB ADM 199).

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[56] See CB ADM 176; also see PX 679; PX 683. Warehouse receivables remained ineligible until September 17, 1971 when they were changed to eligible at the insistence of the Ford Motor Credit Company who wanted to "comply with the ratios in the Ford agreement" (*Waldman Tr.* 1213). At this point Citibank, who was about to receive more than $12 million from the Ford loan and the Private Placement, had "no objection . . . because we were not going to increase the loan balance at all" (*id.*).

III.

FINANCIAL CONDITION OF TOPPER PRIOR TO THE PRIVATE PLACEMENT

A.

Topper's Finances Prior to December 31, 1970

P107. Following substantial losses in 1965 and 1966, resulting in significant measure from Topper's guaranteed sale and bill and hold practices (PX 462, Exh. 1 at 8) Topper's consolidated statement of operations (*id.* at 6-7), certified by Arthur Young and distributed to plaintiffs as part of the Private Placement Memorandum, purported to show substantial improvement, beginning with the eleven month period ending December 31, 1967 and continuing through the fiscal year ending December 31, 1969 (000 omitted):

	1967	*1968*	*1969*
Net Sales	$30,293	$35,036	$53,723
Net Income (or Loss)	($833)	$ 596	$ 2,716

P108. Topper's relative success during the three year period preceding 1970 was the result of a product line which had fared well at retail and thus minimized the need for customer concessions at the rate which prevailed in 1965 and 1966. Thus the amount of credits issued for concessions during the years 1967 through 1969 averaged 14.5% (PX 1435) compared to a 17.2% ratio for 1965 (CB ADM 119). Since each dollar of credits or reserves represented a direct deduction against both sales and profits (*Cook Dep.* 156), a 17.2% ratio of credits to sales in 1967-1969 would have resulted in a net loss for two of those three years.[57]

(c) Topper Falters in 1970

P109. Continuation of this upswing through 1970, or at the minimum avoidance of any return to Topper's prior pattern of losses, was necessary for Topper to keep on raising additional amounts of outside capital required for continued support of its operations (see *Weiss Tr.* 132-34).

P110. The summer and fall of 1970 were particularly significant to Topper's plans, since the toy "business is very seasonal" (PX 1028 at 2) with "shipments during the last half of each calendar year . . . substantially greater than shipments during the first half" (PX 554 at 10); thus in 1968, 77.4% of Topper's sales took place during the six months of June through November (CB ADM 57), and for 1969 the comparable figure ran 75.5% (CB ADM 58).

P111. Anticipating a similar sales pattern in 1970, Topper prepared a projected statement of operations in early January 1970 for the forthcoming year (PX 1366) which was submitted to Citibank and described as "conservative" (*id.* at 4).[58] This statement projected that sales during the months of June through November would amount to 77.6% of Topper's total sales for 1970 (*id.* at 6).

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[57] By applying a 17.2% ratio of credits to gross sales, in place of the actual ratio shown on PX 1435, Topper's net income would have been reduced by $900,000 in 1967, $800,000 in 1968, and by $1,900,000 in 1969.

[58] On October 31, 1969 Topper advised Citibank that it would "probably project sales of $80MM and a profit of $10MM" for 1970 (PX 137).

P112. During the first half of 1970, sales for four of the first six months fell substantially short of projections,[59] even though Topper had previously advised Citibank that sales "for the first quarter of 1970 are expected to be approximately triple the same period" of 1969 (PX 710 at 2). However, Topper's overall sales for this period were in line with the amount projected earlier in the year—*i.e.,* six-month shipments of $17.6 million (CB ADM 62) compared with a $17 million projection (PX 1366 at 6).

P113. Topper met overall projections for the first half of 1970 only by reporting substantial sales during April and May, the two months immediately preceding the June 3, 1970 initial public offering of Topper common stock (PX 1366 and CB ADM 62).

P114. Following its first-half performance, Topper revised its original projections for the remainder of 1970 (PX 673), and submitted these figures to Citibank in late July (PX 672). Significantly, the revised schedule decreased the amount of projected sales for June - November 1970 by more than $9 million (PX 1366 at 6 and PX 673 at 5).

P115. As the second half of 1970 wore on, Topper's toy shipments during the crucial summer and fall months fell significantly short of the "conservative" projections submitted to Citibank at the beginning of 1970. Thus by the end of November, Topper's net sales were $16.3 million below the $68 million projected to Citibank:

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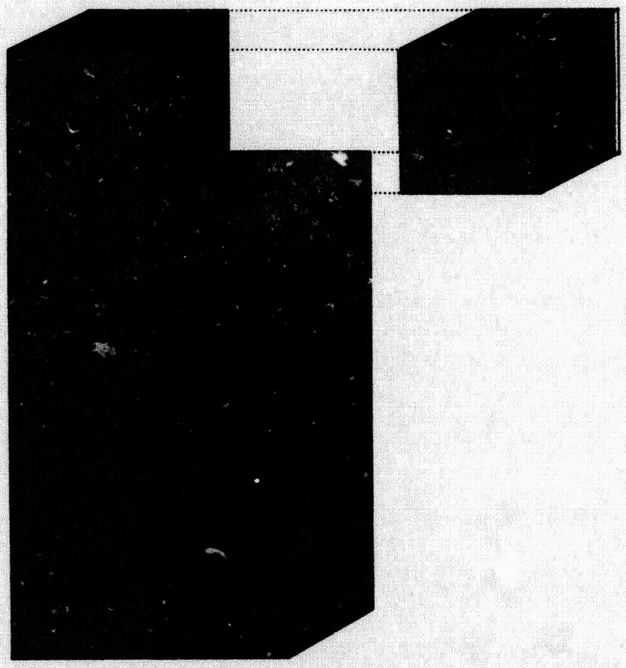
[59] Sales for the months of January, February, March and June 1970 were 71.1% of the amount originally projected (CB ADM 62; PX 1366 at 6).

PX 1432

TOPPER CORPORATION

1970 NET SALES

Original Projection
For Period Ending November 30, 1970



SOURCE: Topper Corporation Consolidated Statement of Operations for the Period January 1, 1970 to November 30, 1970 included within Topper Corporation Consolidated Financial Statements and Supporting Schedules for the Period Ended November 30, 1970 (PX 1170; Citibank Admissions 62 & 1104) and Topper Corporation Projected Analysis of Receivables and Inventories 1970 Estimated included within Topper Corporation Comparative Financial Statements 1966 through 1968 with Projected 1969 and 1970 (PX 1366/CBX 110)

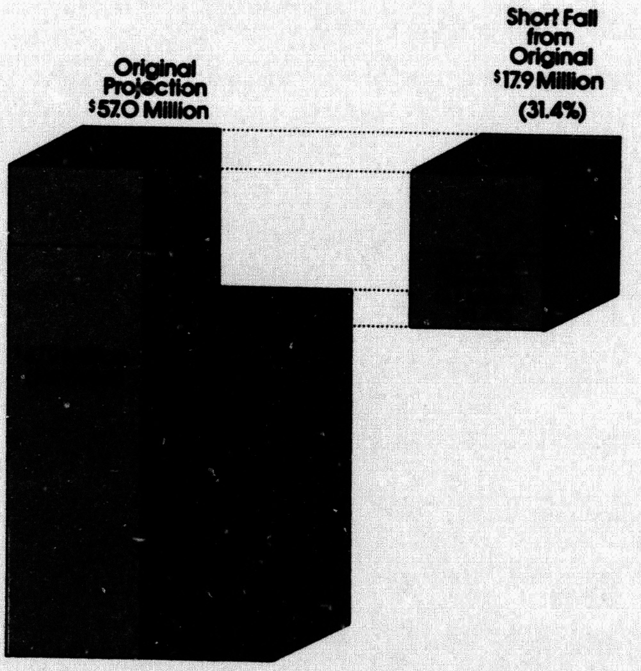
P116. A similar result was evident when actual sales were compared to the scaled-down version of the "conservative" figures revised and submitted to Citibank at mid-year:

PX 1433

TOPPER CORPORATION

1970 NET SALES

Original & Revised Mid-Year Projections
For June 1-November 30, 1970



SOURCE: Topper Corporation Consolidated Statement of Operations pages included within the Topper Corporation (Unaudited) Monthly Consolidated Financial Statements and Supporting Schedules for June-November 1970 (PX 1079, PX 1166-1170; Citibank Admissions 62, 1011, 1100-1104) and Topper Corporation Projected Analysis of Receivables and Inventories 1970 Estimated included within Topper Corporation Comparative Financial Statements 1966 through 1968 with Projected 1969 and 1970 (PX 1366/CBX 110) and Topper Corporation Projected Analysis of Receivables and Inventory for the Period June 1, 1970-January 31, 1971 included within Revised Projections 1970 (PX 673/CBX 111; Citibank Admissions 61 & 602)

P117. Topper's disappointing sales record through the fall of 1970 was attributable to the fact that shipments of two major toy lines were off markedly from both 1969 levels and 1970 projections; thus

(a) the Johnny Lightning line, the most successful Topper product in 1969 (PX 1159 at 24), was down 15.6% in 1970 from 1969 levels (PX 1069 at 31), and off some $13.5 million from the $35.4 million projected earlier in the year after the 1970 Toy Fair (PX 1192); and

(b) the Suzy Homemaker line, the second of Topper's six general lines of product (PX 462 at 6) was off $3.3 million from 1969 (PX 1069 at 28) and down more than 26% from the $8.7 million projected for this line in March 1970 (PX 1192).

P118. Nor was Topper faring any better with its Dawn line of toys and accessories, which by the fall of 1970 had replaced Johnny Lightning as the mainstay of Topper's product line (PX 1170 at 21). Thus as of November 30, 1970 Topper was reporting shipments of Dawn dolls and accessories of $24.1 million (PX 1170 at 21), roughly two-thirds of the $36.9 million projected for 1970 by Topper's sales department on March 19, 1970 (PX 1192 at 1).

P119. Reflecting the failure to meet projected operations, Topper was reporting a loss during the very period when toy operations were traditionally the most successful. Thus Topper's consolidated statement of operations showed a net loss of $348,000 for the month of September 1970, compared with a net income of $1,093,000 for the comparable period in 1969 (PX 1079 at 4); and for the month of October 1970, Topper showed a net loss of $409,000, compared with a net profit of $1,466,000 for the same period in 1969 (PX 1169 at 4).

P120. For the two key months of September and October 1970 alone, then, Topper's net income was off more than $3.3 million from 1969; as a result, at the close of the ten-month period ending October 31, 1970, Topper was reporting a net loss of $78,000, compared with a net profit of $3,056,000 in 1969 (PX 1169 at 7).

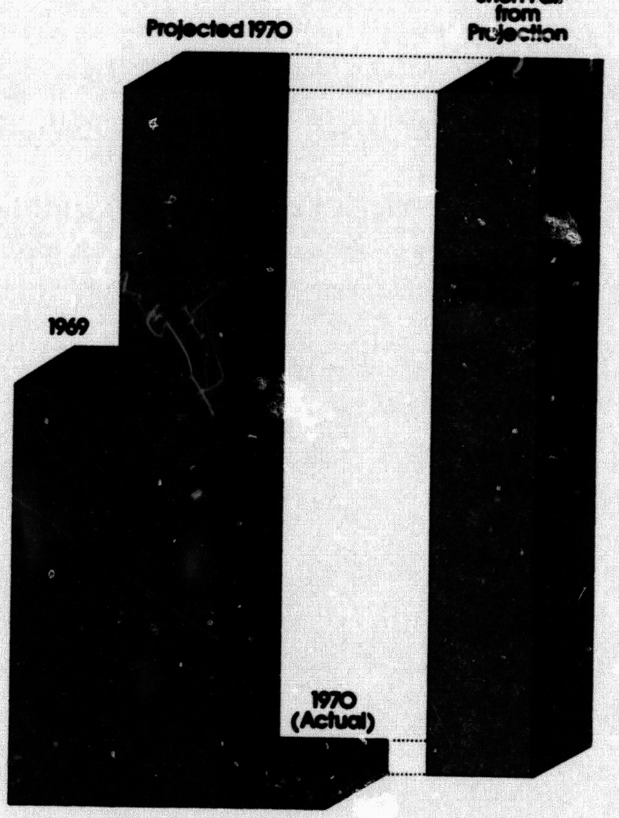
P121. By November 30, 1970, at the close of the period which "for all intents and purposes, for this company . . . can be considered the year end" (*Weiss Tr.* 144), Topper was able to report a profit of only $189,000 off 91.8% from the $2.3 million profit reported for the comparable period in 1969 (PX 1434), and $3.6 million below the net profit anticipated for this period, based on Topper's original 1970 projections (see *Weiss Tr.* 150-53):

PX1434

TOPPER CORPORATION

NET PROFIT (LOSS)

For the Period Ended November 30, 1970.



SOURCE: Topper Corporation Consolidated Statement of Operations for the Period January 1, 1970 to November 30, 1970 included within Topper Corporation Consolidated Financial Statements and Supporting Schedules for the Period Ended November 30, 1970 (PX 1170; Citibank Admission 1104) and Topper Corporation Recast Profit and Loss Statements 1966–1968 with 1969 and 1970 Projected included within Topper Corporation Comparative Financial Statements 1966 through 1968 with Projected 1969 and 1970 (PX 1366/CBX 110)

Findings of Fact

P122. Mirroring the failure of Topper's products at retail was the sharp increase in the amount of credits issued customers for returns, allowances, discounts and other concessions in 1970. In absolute terms, such credits more than doubled from $9 million in 1969 to more than $19 million in 1970 (PX 1435); and as a percentage of all sales, credits increased from the 14.5% level prevailing for the past three years to 23.3% in 1970, a relative increase of more than 60%.

P123. The significance of such increased credits, or this "abberation" as Mr. Weiss of Price Waterhouse described it (*Weiss Tr.* 155), was all too clear: Topper was experiencing a substantial increase in the amount of concessions issued customers for unsold Topper inventory, itself a strong indication of a toy company beset with a product line that had lost favor with the ultimate consumer.[60]

P124. As 1970 drew to a close, mounting problems with the Topper product line had a significant toll on its finances as well. With Topper merchandise failing to sell at retail, Topper customers began withholding payment on their accounts receivable, and Topper's cash collections fell short of projections by more than $6.9 million for the year as a whole (PX 1560). Reflecting the sharp decline which occurred during the last half of 1970, $6.4 million of the $6.9 million shortfall during the year occurred in the last quarter of 1970.[61]

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[60] See Plaintiffs' Findings P77 - P82, *supra* at A80-A83.

[61] This dramatic shortfall was unforeseen as late as July 1970; thus cash collections from customers for the months of June through December 1970 fell short of the revised collections projected in mid-year to Citibank (PX 673) by more than $5.8 million (PX 1560). And $5.3 million of the $5.8 million shortfall was attributable to the months of November and December 1970 alone.

P125. Compounding its difficulties in 1970, Topper "[discontinued] its toiletries operations" which it introduced through its wholly-owned subsidiary, Youth Care, Incorporated, in 1970, and "which incurred a loss in 1970 of $876,164" (PX 462, Exh. 1 at 14).

(ii) *Citibank's Knowledge of Topper's Disappointing Performance in 1970*

P126. As Topper began its 1970 toy year, Citibank recognized that the $2 million net profit reported for the fiscal year ending December 31, 1969 indicated that "Topper, principally due to the continued good acceptance of their products, continues to make substantial improvement" (PX 667 at 1, 4). Along this same line, Citibank noted that Topper's 1970 projections (PX 1366) "provides for further increase in volume to $73.5MM plus $5MM for Youth Care Inc." (PX 667 at 2).

P127. By late July 1970, however, first indications of a less than satisfactory year were reported to Citibank. Thus on July 27, 1970, Topper officers met with Citibank officials "to preview their new toy line for next year and to receive and review their revised cash projection" (PX 672). It was this set of revised projections (PX 673) which scaled down the prior and "conservative" version submitted to Citibank in January.[62] In light of this revision Citibank viewed Topper's request for additional cash requirements —occasioned by the fact "that they did not receive monies from stock issue as anticipated and collections due to additional datings have not come in as projected" (PX 672 at 1) —with skepticism:

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[62] See Plaintiffs' Finding P114, *supra* at A97.

> "Furthermore, an increase in their line due to non receivable collateral is not justified due to a decrease in anticipated sales and profits. Not knowing whether or not client will need additional line (due to 30 day acceptances) suggest they make every effort to speed collections" (*id.*).

P128. Such skepticism proved warranted, for by October 30, 1970 Topper management was expressing concern to Citibank "regarding their ability to meet projected volume" (PX 674); the best estimate was "that they will be several million short" (*id.*).

P129. More significantly, Citibank was informed at the end of October that Topper's Dawn line was falling short of expectation and that credits for customer concessions were running proportionately higher in 1970 than in 1969:

> "Concerned regarding their ability to meet projected volume. Best estimate now is that they will be several million short. Expect to also be several million short of the Dawn Doll orders at year-end.
>
> "The latter is a paradox as the Dawn Doll is the best selling item (wholesale and retail) because of its low cost and price. While the higher priced items, i.e., Suzy Homemaker Fashion Show and Johnny Lightning Race Car Sets have slowed down.
>
> • • •
>
> "The proportionately higher discounts and allowances given this year vs. last year, were primarily motivated to book sales (cash generation) on the higher ticketed items" (PX 674).

P130. In fact Citibank was aware that credits for customer concessions had more than doubled as percentage of gross sales from 1969 to 1970. Thus a Citibank audit report for 1970 stated:

> "Gross sales for the year 1970 were 74MM as compared to 59MM in 1969—however dilution and turnover both went up; dilution mainly because of advertising allowances and more liberal return privileges—turnover because of more extended datings.
>
> • • •
>
> "Dilution is understated as client issues many 'credit-debit' invoices for transfer billing . . . and certain adjustments. Dilution is close to 18-20% (estimated)" (PX 700 at 1-2).

P131. Again on December 1, 1970 Citibank was advised of [illegible] faltering operations when Orenstein telephoned Mr. Waldman to report "he was quite disappointed" with "current sales efforts" (PX 746). According to Mr. Waldman, "Orenstein is preparing us for a season which will not wind up according to his earlier projections" (*id.*).

P132. Finally, on December 22, 1970, Topper informed Citibank that as a result of slow toy shipments prior to Christmas, "they will require a substantial over-advance" (PX 675 at 1). Although Citibank believed its loan was "reasonably secured" (*id.* at 2), Citibank thought that its own reserve "for returns and deductions" should "be followed closely and we are to be satisfied at all times that our reserve is adequate" (*id.* at 1). As a result, as 1970 drew to a close, Topper was a company which Citibank thought should "be watched very closely due to the uncertainty of the economic climate and the inherent problems in the Toy Industry" (*id.* at 2).

P133. According to a representative of the Ford Motor Credit Company, Siegel's concern with the Topper account in fact began with "the cash shortage beginning in . . . the latter part of 1970" (*Skaar Tr.* 1343), a shortage amounting to more than $6.4 million during the last three months of the year (PX 1560).

B.

Extended Dating Sales of $16 Million in December Enable Topper to Report a Profit for 1970

P134. Absent any unusual pattern in December, Topper's financial fortunes in 1970 should basically have been set by November 30; according to Mr. Weiss of Price Waterhouse, "if you don't make it in November . . . at least in this industry . . . you just don't make it" (*Weiss Tr.* 145).

P135. Based on past experience, the prospects for any substantial amount of sales in December were bleak, since the lead time required for a manufacturer to ship merchandise to the stores for the Christmas season disabled toy sales by manufacturers during the month of December (CB ADM 98). The "last effective date [toys] could be shipped or would be shipped to reach the Christmas market", according to the Citibank official responsible for the Topper account, "would probably be in October" (*Waldman Dep.* 36-37).[63]

P136. Contrary to this established pattern, sales in December 1970 accounted for 21.4% of Topper's net sales for the year:

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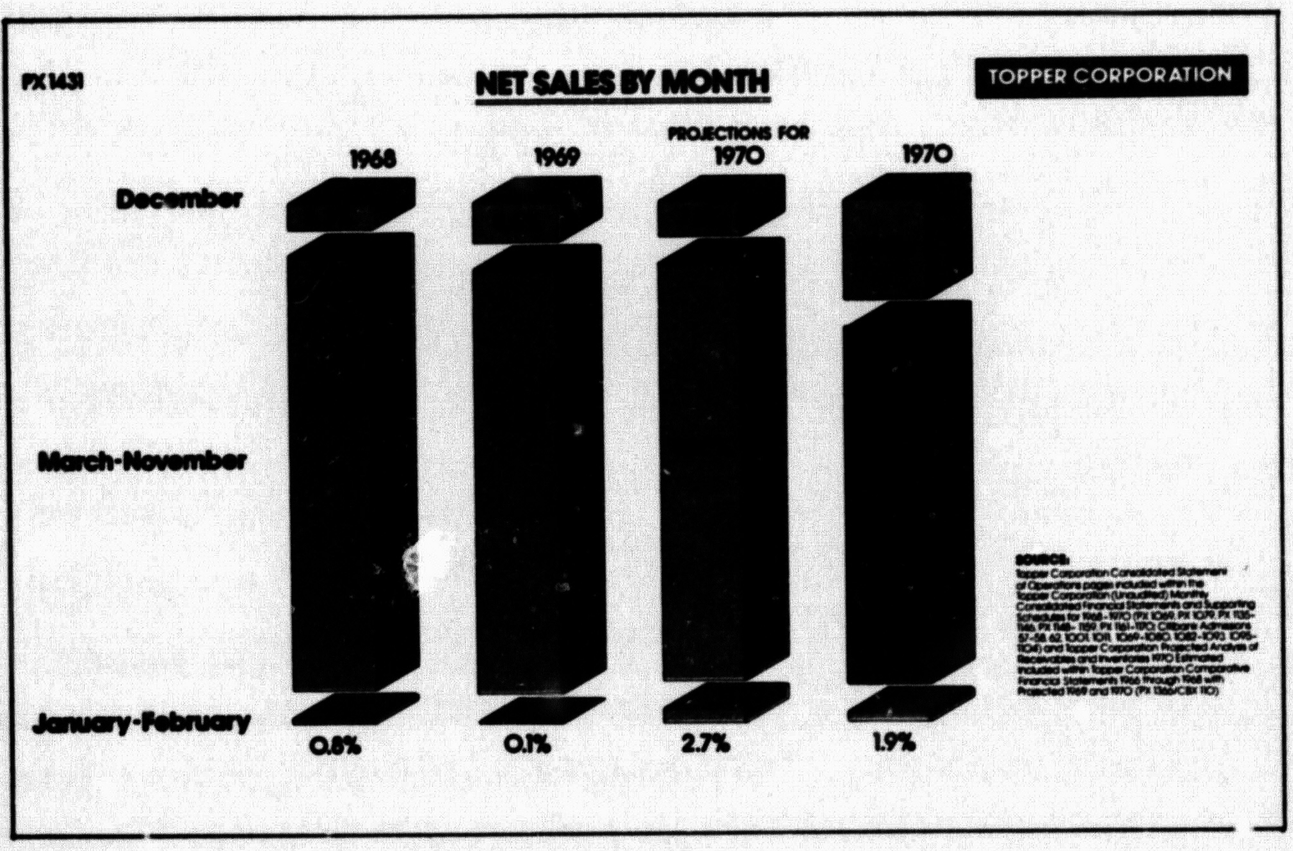
[63] While 77.4% of Topper's sales in 1968 took place during the months of June through November, only 5.3% occurred in December (CB ADM 57); likewise, while 75.5% of Topper's sales occurred during June-November 1969, only 8.6% occurred in December of that year (CB ADM 58).



SOURCE:
Topper Corporation Consolidated Statement of Operations pages included within the Topper Corporation (Unaudited) Monthly Consolidated Financial Statements and Supporting Schedules for 1968 - 1970 (PX 1069; PX 1079; PX 1135-1146; PX 1148-1159; PX 1161-1170; Citibank Admissions 57-58, 62, 1001, 1011, 1069-1080, 1082-1093, 1095-1104) and Topper Corporation Projected Analysis of Receivables and Inventories 1970 Estimated included within Topper Corporation Comparative Financial Statements 1966 through 1968 with Projected 1969 and 1970 (PX 1360/CBX 110)

(i) *The Spring 1971 Program*

P137. Topper achieved this remarkably high level of sales in December by embarking on what a partner of Arthur Young described as "an unusual program" (*Walsh Dep.* 43) never tried "on a material scale before" (*id.* at 42). Under this program, known as the Spring 1971 Program, customers were invoiced approximately $16 million of toys in late December 1970 on extended credit terms of five to eight months (PX 332; CB ADM 91).

Findings of Fact

P138. After allowing for reserves of $2 million,[64] the Spring 1971 Program accounted for approximately 22% of Topper's net sales for the fiscal year ending December 31, 1970 (CB ADM 93). This compared with the approximately $2 million in extended dating sales logged in December 1969, which comprised less than 4% of that prior year's sales (*id.*).

P139. Sales reported by Topper for the month of December 1970 were also substantially in excess of the amount previously projected for this month. Thus Topper initially estimated in early January 1970 that December sales of $5.5 million (PX 1366 at 6) would comprise only 7.5% of total sales for the year; in fact they amounted to 22% (CB ADM 93). December sales were also significantly greater than the amount of the revised projections submitted to Citibank in late July 1970 which estimated December sales running only 11.8% of sales for the year (PX 673 at 3, 5).

P140. According to Topper, the purpose of the Spring 1971 Program "was to encourage and promote sales by . . . customers in the early part of the year" and thus even out sales "throughout the year as a whole" (*Orenstein Dep.* 106; CB ADM 96); as Topper advised Citibank, it was "obliged to give special dating" in order "to attract business for early 1971" (PX 718 at 1).

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[64] According to Topper approximately $1.5 million was reserved for goods stored in a warehouse situated in the New York Terminal Warehouse (CB ADM 164) and an additional $400,000 was reserved for special discounts granted to franchise distributors (PX 1021; *Zoll Dep.* 121-23). According to Arthur Young, the reserves were designed to protect against "returns or concession[s]" applicable to the entire Spring 1971 Program (*Botte Dep.* 39-41) and were created as a result of Topper's past "experiences" when they sold "toys to supermarkets on a guaranteed sales basis" (*Cook Dep.* 96-97).

P141. The great bulk of merchandise invoiced under the Spring 1971 Program was comprised of the Dawn line of toy dolls and accessories introduced at the 1970 Toy Fair (PX 462, Exh. 1 at 10-11). In the brief period from April through December 1970, Topper shipped over $41.4 million in Dawn dolls and accessories (CB ADM 56), which comprised roughly two-thirds of Topper's net sales for 1970 (see PX 1430).

P142. According to the Private Placement Memorandum, Topper sold approximately $11 million of the Dawn line under its December program (PX 462 at 6); in truth, Topper's own records showed $17.3 million of Dawn shipments for the month of December alone (cf. CB ADM 56 and PX 1170 at 21).

P143. The $17.3 million of Dawn shipments in December 1970 were made despite warnings from principal distributors that Dawn was already overstocked on retail shelves, the very "paradox" which Citibank itself observed two months earlier at the end of October 1970 (PX 674).[65] Thus:

(a) a major distributor in the New York area, Greenman Brothers, returned a large shipment of Dawn items at the end of November because it "had enough of it in stock" and "figured at that point we would not sell that out by Christmas" (*Greenman Tr.* 309-10; see PX 1319);

(b) another west coast distributor reported a "tremendous carryover" of almost $400,000 in Topper inventory, including "60% or more . . . in the Dawn category", and asked Topper to "cooperate with us in seeing to it that we do not have a burdensome problem" (PX 841); and

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[65] **See Plaintiffs' Finding P129, *supra* at A105.**

(c) a Minneapolis distributor of Topper products testified he told Topper that a proposed Dawn order represented "far too much merchandise, especially in view of the fact that it was ordered in December, after the Christmas season", and will "be unlikely to be used in any kind of quantity until much later in the year 1971 . . . that it probably wouldn't sell and that [we] would have to return it" (*Sieff Dep.* 52); as a result, this customer told Topper the Spring 1971 Program "was a very big gamble on their part and they were liable to end up with an awful lot of merchandise" (*id.*).

P144. Heightening customer concern over Topper's massive Dawn shipments at the end of December were Topper's plans to effectively supersede its 1970 Dawn line with a large number of newly designed items which, within two months of the program, would be advertised and promoted as "even more spectacular" (PX 920 at 44) than the $16 million in goods sold in December 1970.[66]

P145. To overcome the reluctance of customers to accept large quantities of merchandise at the close of the 1970 Christmas season (*Sieff Dep.* 51-52), as well as their reluctance to accept 1970 merchandise which would have to compete with newly designed toy items in two months or so, Topper, among other things, offered a 10% "bonus" discount to customers participating in the Spring 1971 Program. They did so, Topper's Vice President-Sales testified, "to encourage the customers to give us large orders" in December 1970 when the toy season had effectively passed, and "to make it worth their while to buy more merchandise than they would buy normally" at this time of year (*Pierce Dep.* 13).[67]

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[66] In light of this fact, Topper customers demanded, and management granted, the right to exchange 1970 toys for those introduced in 1971; see *e.g.*, PX 838, 840, 873, 874, 876, 878, 885, 886, 887, 888, 890, 891, 892, 893 and 897.

P146. In a further effort to overcome customer reluctance to participate in the Spring 1971 Program, Topper informed distributors that its general practice of "protecting" them against unsold inventories would apply as well to the Spring 1971 Program.[68] Thus:

(a) one distributor who acknowledged that the program was "tantamount to a guaranteed sale" (*Greenman Tr.* 320; PX 1324) agreed that "the terms relating to that transaction were no different than the terms relating to the other dealings" he had with Topper (*Greenman Tr.* 321);

(b) likewise another customer who was told "that there wouldn't be any risk" because he could "exchange any merchandise that slowed down in sales" (*Monchik Tr.* 181) also agreed that this was an "arrangement that had been existing all the time" (*id.* at 197); and

(c) a third customer who was told that this was a "guaranteed sale" and that he "would never have to pay for it unless we used it" (*Sieff Dep.* 55-56) agreed to participate because of "similar previous courses of dealing with Topper Corporation" (PX 1258; *Sieff Dep.* 49-56).

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[67] Mr. Orenstein agreed, "because they were all anxious to hold back as much as possible until Toy Fair when they saw additional items" (*Orenstein SEC Tr.*, June 21, 1972, at 40).

[68] See HSX Schwartz R; PX 852, 915, 896, 1351, 849, 895, 888, 891, 881, 876, 883, 1353, 885, 890, 878, 887, 873, 1354, 886, 892, 874, 840, 1352, 893, 838, 1359 884, 844, 907, 908, 1333.

P147. In mid-December Orenstein outlined the "general approach of the spring program" (*Pierce Dep.* 17) for his sales force, instructing them to stress the bonus discount feature as well as the "no risk—no money" aspects of the Program. Thus notes taken during the course of a December 18, 1970 conference between Orenstein and two senior sales officers reflect:

> "*H.O.* *12-18-70*
>
> "Spring Deal Approach
> "Don't Plead for order—
> A one time Discount Never Repeat
>
> "(1) Customer gets best deal ever had
> *no risk*—no money—additional disc
>
> "(2) 10% more in buying than they can ever
> make in selling (2%)
>
> "(3) A big pie (profit) my customers to be
> competitive and have a bigger piece of
> the pie.
>
> An enormous buying advantage. Buy all new
> mdse at a very competitive position
> Can't afford to pass it by. If they do
>
> A chance to make $1,000 or $10,000
> Every possible protection.
>
> Unusual savings on a no risk category" (PX 852).

P148. The campaign to secure customer orders in December 1970 apparently bore fruit, for in the final nine working days of 1970 Topper reported more than $8.6 million in sales (PX 1061), an amount substantially greater than it was able to report for any other single month of 1970, including the traditionally heavy shipment months of June through November (CB ADM 62).

P149. More striking was the fact that during the last four days of 1970 Topper reported at least $6.3 million, or 10% of its sales for the entire year, with $4 million, or 6%, coming on December 31, 1970 (CB ADM 94). These year-end sales were part of the "drop ship" portion of the Spring 1971 Program under which $10 million in Dawn dolls and accessories were placed aboard ships leaving Hong Kong in late December (PX 1061; CB ADM 94),[69] at least two months late for any possible sale during the 1970 Christmas season (PX 1117 at 1).

P150. Even with the bonus discount and "no risk—no money" features, customers were reluctant to participate in the Spring 1971 Program. As a result, Topper agreed to warehouse approximately $7 million of merchandise under terms similar to the "bill and hold" practices adopted in 1965.[70] According to Topper's Vice President—Sales, warehousing was a "sales tool" which became an essential part of the Spring 1971 Program when Topper customers whose orders were solicited expressed concern over "inventory" problems at year end 1970 (*Pierce Dep.* 13-14)—"some of the customers indicated to us that they just didn't have the facilities to handle that rapid a growth" in inventory (*id.* at 226). To further encourage sales, then, Orenstein authorized " a substantial increase in the amount of warehousing for the 1971 Spring Program" (*id.* at 227).

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[69] Actually $329,000 of this amount left the Orient on January 1, 1971, but was included in 1970 sales on the theory that New Jersey time rather than Hong Kong time prevailed (PX 1062). Customer agreements, however, typically provided that title would pass one day out of port (*e.g.*, PX 474 at ¶ 5), so it was a 1971 transaction under either theory. (See *Walsh Dep.* 119-21, 366-68.)

[70] PX 462, Exh. 1 at 8.

(ii) *Significance of the Spring 1971 Program to Topper's 1970 Financial Statements and Its 1971 Operations*

P151. As a result of treating the Spring 1971 program as a 1970 event, Topper was able to report a net profit for the fiscal year ending December 31, 1970 of $353,000 (PX 462, Exh. 1 at 6-8). Even so, this $353,000 profit was substantially short of the $2,867,000 profit projected to Citibank in early January 1970 (PX 1366 at 4) as well as the $1,676,000 profit anticipated in the revised projections submitted to Citibank in late July 1970 (PX 673 at 2).

P152. According to Mr. Weiss of Price Waterhouse, the $16 million in "extended dated sales contributed approximately $6,500,000 to net profit for the year 1970. Without the extended dating sales . . . they would have suffered a substantial loss in the year 1970" (*Weiss Tr.* 784-85), a loss in fact exceeding some $6 million *(id.)*.

P153. However, the fact of such loss itself was not apparent from Topper's 1970 financial statements themselves, since Topper failed to disclose the amount or significance of credits and their application to operations or the Spring 1971 Program, the basic factor responsible for determining the profit or loss in any given year.[71] Other factors material to determining profitability were likewise unknown.[72]

P154. Underscoring the significance of the relationship between credits and sales, if Topper had maintained the 14.5% ratio of concessions to gross sales in 1970 which prevailed in the 1967-1969 period (PX 1435), rather than the 23.3% rate which actually occurred, it would have realized a net profit of more than $7.3 million in 1970 *(id.)*.[73]

(iii) *Topper's Failure to Disclose The Circumstances Surrounding, Or The Salient Features of, Its Spring 1971 Program*

P155. Only the barest outline of the Spring 1971 Program was disclosed to plaintiffs in connection with the Private Placement. Thus the April 29, 1971 Prospectus stated simply that "December 1970 sales included approximately $14,000,000 of shipments, which consisted primarily of spring program merchandise, carrying extended terms of five to eight months, compared to similar sales of approximately $2,000,000 in 1969" (PX 462, Exh. 1 at 8).

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[71] See Plaintiffs' Findings P78 - P82, *supra* at A80-A83.

[72] **As Price Waterhouse explained:**

> "You don't know the gross profit rate of the extended dated sales from the footnote. You can just try and assume what the extended gross profit rate is from the cost of sales information presented and the sales information presented. So that is not readily discernible. Plus, in addition, there are certain other operating expenses that affect net income. You don't know what the effect of those operating expenses had on those extended dated sales, whether they could apply to them or not. . . . [F]or example, advertising, which is a considerable part of Topper's expense was applicable against the extended dated sales, if you believe it would have some effect, then you would come up with a lower gross profit margin. You would not realize the total effect of the extended dated sales had on net profits" (*Weiss Tr.* 786-87).

[73] See Plaintiffs' Findings P82, P108, *supra* at A82-A83, A95-A96.

P156. Whether this information standing alone was, as the Court inquired, "a healthy or unhealthy sign" depended, as Mr. Weiss of Price Waterhouse pointed out, "on what the toy is and when it was delivered" (*Weiss Tr.* 141):

(a) here the toy was Dawn, an item consistently portrayed to the investing public as highly successful as late as August 1971;[74]

(b) in terms of when the merchandise was delivered, the April 29, 1971 Prospectus specifically stated the program involved "December 1970 . . . shipments" (PX 462, Exh. 1 at 8); there was no indication that $13 million of the Program was shipped at the end of December, rather than in early December for sale at Christmas;

(c) and in terms of the type of sale involved "one could infer that they [were] final or that there [was] a reasonable chance of their collectibility" (*Weiss Tr.* 777), because there was nothing "that would indicate that these sales were consignment sales" (*id.* at 779); if they were "consignment sales and the reliability of the sales were unknown, they should not have been recorded as sales in the 1970 financial statements" (*id.* at 777).

P157. Apart from whatever inferences or assumptions a reader of Topper's prospectus might reasonably draw with respect to the Spring 1971 Program, undisclosed to any plaintiff, in plain words or substance, were any of the material circumstances surounding, or the salient features of, the Spring 1971 Program, including among other things:

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[74] See Plaintiffs' Findings P24 - P27, *supra* at A55-A57.

(a) that the Spring 1971 Program in fact amounted to $16 million, and that reserves and accruals of approximately $2 million had been established to protect against returns and concessions;[75]

(b) that prior to reporting $16 million in sales under the Spring 1971 Program Topper had fallen short of its 1970 sales projections by $16.3 million (PX 1432) and short of its anticipated net profit by $3.8 million (PX 1434);

(c) that without the Spring 1971 Program Topper would have reported a substantial loss for the fiscal year ending December 31, 1970;[76]

(d) that to overcome customer reluctance to participate in the program, Topper had promised a "bonus" discount of 10% to customers who ordered prior to December 31, 1970;[77]

(e) that only $3 million of the $16 million in sales were "actually shipped to customers in December 1970" (*Weiss Tr.* 775);

(f) that merchandise reported as sold under the Spring 1971 Program was subject to returns or other concessions in the event customers were unable to sell such merchandise;[78] and

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[75] See Plaintiffs' Findings P137 - P138, *supra* at A109-A110.

[76] See Plaintiffs' Findings P151 - P152, *supra* at A116.

[77] See Plaintiffs' Finding P145, *supra* at A112-A113.

[78] See Plaintiffs' Finding P146, *supra* at A113-A114.

Findings of Fact

(g) that $7 million of the sales involved merchandise stored under terms comparable to the "bill and hold" arrangements undertaken in 1965, which resulted in the return of approximately $4.2 million of the $7 million in merchandise sold.[79]

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[79] See Plaintiffs' Finding P70, *supra* at A76-A77.

C.

Financial Developments During the First Six Months of 1971

P158. Beyond the impact on Topper's 1970 financial statements, the Spring 1971 program was of particular significance to Topper's 1971 operations as well. Topper, according to Mr. Weiss of Price Waterhouse was "to a very significant extent . . . looking to the 1970 extended dating program to support [its] operations in 1971" (*Weiss Tr.* 787). "Topper had projected that it would need certain amounts of cash to both run its operation and pay down its debt. It was extremely important to Topper to collect most of these receivables" because "you can't operate in 1971 unless you could collect the receivables due from the sales in 1970" (*id.* at 786).

P159. With the accounting judgment to include December extended dating sales in 1970 operations behind it, Topper's concern for 1971 focused on the issue of collections. As Mr. Weiss of Price Waterhouse explained, "the problem of receivables is one of collection. What we have to concern ourselves with is the ultimate collectability of these receivables. It is nice to make the sale, but it is nicer to receive the money" (*id.* at 783).

P160. Collecting these receivables in 1971 meant, for all practical purposes, collecting Dawn receivables, since, according to Citibank, 80% of Topper's outstanding receivables in early 1971 represented Dawn dolls and accessories (PX 718 at 2). In light of Topper's sales and marketing practices, collection of Dawn receivables in 1971 in turn required the type of year-round sale at retail which the program was designed to accomplish.[80] According to Mr. Weiss of Price Waterhouse, Topper in fact "projected collections of these receivables" (*Weiss Tr.* 786) in 1971, principally during the months of May through September (*id.* at 793).

P161. With its financial fortunes dependent in principal measure upon the success of the Dawn line, Topper began 1971 planning only one outside financing to support toy operations for the coming year (CB ADM 70); the single financing was occasioned by the substantial shortfall in collections which occurred at the close of 1970.[81] Thus a January 21, 1971 Projected Statement of Operations for the period ending December 31, 1971 forecast cash receipts of $74,950,000 (PX 6 at 5) and customer collections of $71,950,000 (*id.* at 6). The difference between projected receipts and collections represented a single offering of common stock targeted for May and scheduled at that time to net $3 million (*Rose Dep.* 593-94).

P162. Within a month of these projections, however, serious questions relating to Topper's financial assumptions for 1971—questions first raised in December 1970 when principal customers reported excess Dawn inventories prior to Christmas[82]—were raised anew, this time on a broader scale at the 1971 Toy Fair. Thus in early February 1971, Topper customers again reported a heavy build-up in inventories of Dawn (CB ADM 71). For example, one major customer advised Topper on February 9, 1971 that the "carryover on Dawn" was "tremendous" (PX 875). Testifying on this report, Topper's Vice President-Sales acknowledged that during "[this] time frame" customers were expressing concern about "how long it would take them to sell" Dawn merchandise (*Pierce Dep.* 25-26).

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[80] See Plaintiffs' Finding P140, *supra* at A110-A111.

[81] See Plaintiffs' Finding P124, *supra* at A103.

[82] See Plaintiffs' Finding P143, *supra* at A111-A112.

P163. Confirming the Dawn build-up, Topper agreed in early 1971, according to Arthur Young (*Cook Dep.* 296-300), to redate or extend at least $3.3 [million] in receivables,[83]

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[83] "At least" appears justified because evidence of early 1971 redatings are available for only 12 of Topper's seven hundred customers. Such documents show, however, the following receivable balances as of December 31, 197[0], and of such receivable balances, the following amounts redated or otherwise extended in January and early February of 1971 (000 omitted):

	Customer	*Receivable Balance as of December 31, 197*[0]†	*Amount Extended or Redated*††
1.	American Leisure	$1,048,000	$ 704,000
2.	Barkers	245,000	138,000
3.	AYR Stores	254,000	127,000
4.	Consolidated Athletic	338,000	338,000
5.	Federal Warehouse Co.	596,000	28,000
6.	National Merchandising	160,000	110,000
7.	Pensick & Gordon	726,000	350,000
8.	A. Ponnock	549,000	518,000
9.	S & H Wholesale Co.	177,000	107,000
10.	Southland Distributors	183,000	71,000
11.	Vornado	1,077,000	547,000
12.	Halco	283,000	283,000†††
		$5,636,000	$3,321,000

† Information derived from PX 1064 at 2

†† For the amount or extent of redating, see PX 1063.

††† This figure is from PX 918.

over 80% of which were comprised of Dawn (PX 718), which customers had been unable to sell during the 1970 Christmas season. Topper formally redated by way of four letters dated March 24, 1971, $2.2 million of receivables originally due January 10, 1971, pursuant to agreements reached at the 1971 Toy Fair (CB ADM 187; PX 922).

P164. At the same time Topper customers were reporting a build-up in Dawn inventories, Topper recognized that its operations for 1971 would require raising even more working capital from outside investors. Accordingly within a month of its original projections, on February 23, 1971 Citibank was informed that beyond the public offering set for May, which had been expanded to raise $5 million instead of the original $3 million (PX 678), Topper was considering a second financing in 1971, to take place after the May public offering and to consist of $5 million in "ten year term money from an insurance company" (*id.*; CB ADM 73).

P165. As the first quarter of 1971 came to a close, and Topper prepared for its April 29 public offering, Topper reported net sales of $4.9 million for the three-month period ending March 31, 1971, compared with net sales of $2.0 million for the first quarter of 1970; and a net loss of $398,000 compared with a net loss of $1.0 million for the comparable period in 1970 (PX 462, Exh. 1 at 9).

P166. In significant measure, however, the improved first quarter results reported by Topper just prior to the April 29, 1971 public offering were attributable to the fact that to induce increased sales during this period, Topper:

(a) agreed at the 1971 Toy Fair to redate or extend the due date on a substantial amount of receivables representing merchandise which customers or retailers had been unable to sell during the 1970 Christmas season (CB ADM 187; PX 1067).[84]

(b) "continued to sell a substantial amount on extended dating terms in 1971" (PX 1058 at 2; CB ADM 102), at least 30% of merchandise reported as sold during this quarter (PX 1057); and

(c) warehoused an additional $1 million under bill and hold arrangements for customers unwilling to accept delivery at the time Topper was reporting a sale (PX 1000).[85]

P167. Moreover by March 31, 1971, 44% of the $16.5 million in non-Spring 1971 Program receivables reported on the December 31, 1970 Topper balance sheet of Topper, which for the most part represented Dawn merchandise shipped for the 1970 Christmas season and which was due for payment on January 10, 1971, had not been collected from customers (PX 1058 at 2; CB ADM 74).

P168. By April is became clear that the avowed purpose of the Spring 1971 Program, namely to enable sale of the low priced and non-seasonal Dawn merchandise during the first months of the year[86], had and would not be achieved (CB ADM 75). The effect of this development on Topper's cash flow for the balance of 1971 was readily apparent. Thus on April 23, 1971 Topper's finance department was informed that receivables related to unsold Dawn merchandise would be paid for only as the items themselves were sold at retail (PX 1093). As Topper subsequently informed Arthur Young:

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[84] See Plaintiffs' Finding P68, *supra* at A76.

[85] See Plaintiffs' Findings P69 - P76, *supra* at A76-A79.

[86] See Plaintiffs' Finding P140, *supra* at A110-A111.

> "By 5/71 spring program merchandise not moving as quickly as anticipated. For customers whose merchandise not moving well general understanding with sales dep't that payment would be due when merchandise was sold by customer" (PX 1091 at 1).

P169. The failure of Topper's Dawn line to retail as anticipated during the first half of 1971 was more clearly evident with respect to Dawn merchandise stored in the New York Terminal Warehouse. Thus on May 14, 1971 a Topper officer observed, "it apears that we can expect long stretch-out in payments" on merchandise stored in the New York Terminal Warehouse (PX 501). This "stretch-out", the officer explained, was quite apart from the "pay as sold" agreements made with respect to the Spring 1971 Program generally:

> "For instance, it has been confirmed by the salesmen that in the case of Circus World and Alpeg, agreement is that payments will be made 100 days from date of any partial withdrawal.
>
> "This is a situation quite apart from agreements made on spring deal shipments direct to customers but which payments [are] made upon salesmen inventorying accounts to see how much has been sold. Payment then is made for that amount" (PX 501).

P170. More significant than the "stretch-out" in payments was the outright return of substantial amounts of Dawn merchandise by Topper distributors beginning in early spring 1971.[87] Reflecting this, two of the three customer witnesses testifying at trial acknowledged substantial Dawn returns during the period April through June 1971:

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[87] See PX 1198, 839, 1321, 1326, 1327, 1328, 1329, 1330, 1331, 1332, 1204, 910, 805, 905, 904.

(a) the President of one such customer, Irving Monchik of Shepher Distributors, testified that during these months his company returned $445,000 of the $660,000 in Dawn dolls and accessories purchased under the Spring 1971 Program (*Monchik Tr*. 183-90); according to Mr. Monchik, he realized within "three or four months" in 1971 that the Spring 1971 Program "never really materialized the way they had programmed it, and I was beginning to get uneasy that I had far too much merchandise at the rate it was moving and I began to start the ball rolling in relation to returning some of the so-called merchandise which I realized was in excess" (*Monchik Tr*. 184); and

(b) a second customer, Greenman Brothers, informed Topper in early May 1971, that it planned to return Dawn dolls and accessories with an invoice value of approximately $168,000 (PX 1323; cf. PX 1450 at 3, PX 1453 at 6); this same customer wrote Topper on July 29, 1971 via registered mail that it decided "to hold up all payments and all incoming shipments" until Dawn and other merchandise valued at roughly $150,000 was returned (PX 1324; cf. PX 1450 at 3, PX 1453 at 6; PX 1039); only when credits were issued for "the return of this merchandise", Greenman Brothers stated, would it be in a position to pay for the balance of its Spring 1971 Program purchases (PX 1324).

P171. The failure of Dawn to retail as originally anticipated, and the related decisions to permit customers to return unsold merchandise or allow them to withhold payments until the goods were sold at retail, intensified Topper's impending cash needs for its continuing operations (*Weiss Tr.* 836-41).

P172. To meet such needs, Topper increased the number of proposed financings from outside investors once more in early spring 1971. Thus Topper, which anticipated a single offering just three months earlier,[88] was by April planning the soon to be consummated common stock public offering. Beyond this offering, Hayden Stone was engaged in early April 1971 to review "the feasibility of raising $5 million for the company through an issue of long term straight debt or debt with warrants" (PX 579 at 1). Finally, the same time Hayden Stone was laying the groundwork for the Private Placement, Topper began negotiating for a $7 million loan from the Ford Motor Credit Company (*Pompea Dep.* 14).

P173. For the six month period ending June 30, 1971, Topper reported net sales of $19.3 million and a net profit before provision for federal income taxes of $590,000 (PX 2 at 4). Like its first quarter financials, however, the results of operations for the first six months of 1971, distributed to the Pension Fund and Connecticut Mutual prior to the Private Placement,[89] unfairly presented Topper's true financial condition at June 30, 1971, in that:

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[88] See Plaintiffs' Finding P161, *supra* at A122.

[89] The first significant decline in Topper's operations in 1971 was reflected in Topper's unaudited monthly financial statement for the seven months ending July 31, 1971 (PX 3 at 5), a document never shown any plaintiff prior to the Private Placement. This statement reported a decline in net sales of $3.3 million for the month of July 1971 from the comparable period in 1970, re-

(a) $4.9 million of the $19.3 million in sales, or more than 25%, represented bill and hold merchandise stored in the New York Terminal Warehouse which customers were under no obligation to withdraw;[90]

(b) more basically, $11.5 million, or roughly 60% of the $19.3 million in reported sales, comprised Dawn dolls and accessories, a toy line whose failure to retail as anticipated had been clear since the beginning of the year,[91] and which was currently being returned in substantial quantities by overstocked customers; and

(c) 50% of the $29 million in receivables shown on the June 30, 1971 balance sheet (PX 7), were listed as not "current" on Citibank's June 30 audit report (PX 702 at 8; see *Siegel Tr.* 1176).

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sulting in a net loss of more than $360,000 for the single month of July. Topper's July 1971 loss wiped out more than 60% of the net profit reported in the June 30, 1971 Financial Statements (PX 2 at 5).

[90] See Plaintiffs' Finding P76, *supra* at A79.

[91] See Plaintiffs' Findings P162 - P163, *supra* at A122-A124.

D.

The Financial Crisis at Topper During the Summer of 1971

P174. According to Mr. Weiss of Price Waterhouse, the months May through September 1971 were of "special significance to Topper", for "to evaluate the success of the Spring Program, we have to basically evaluate it by looking at the collections actually received during this period because this is the period in which these collections became due" (*Weiss Tr.* 793).

P175. Approximately $9.6 million of the extended dating sales were due for payment on May 10, 1971 and the remaining $6.4 million were due on August 10 (PX 332). Collection of these dated receivables was required not only to support 1971 operations; collectibility of the receivables bore significantly as well on the integrity of Topper's 1970 financial statements (*Weiss Tr.* 784-85). But Topper in fact had "projected collections of these receivables" during this period (*id.* at 786).

P176. As the summer of 1971 wore on, however, and the date for payment of the extended dating receivables came and passed, it was evident[92] that Topper had failed to collect receivables as planned in its cash flow projection for 1971 (PX 6). According to a schedule prepared by Topper's Senior Vice President-Finance (PX 393; *Rose Dep.* 27), actual cash collections from customers for the key period May through September 1971 fell short of projected collections for this period by more than $10 million (CB ADM 65 and 66):

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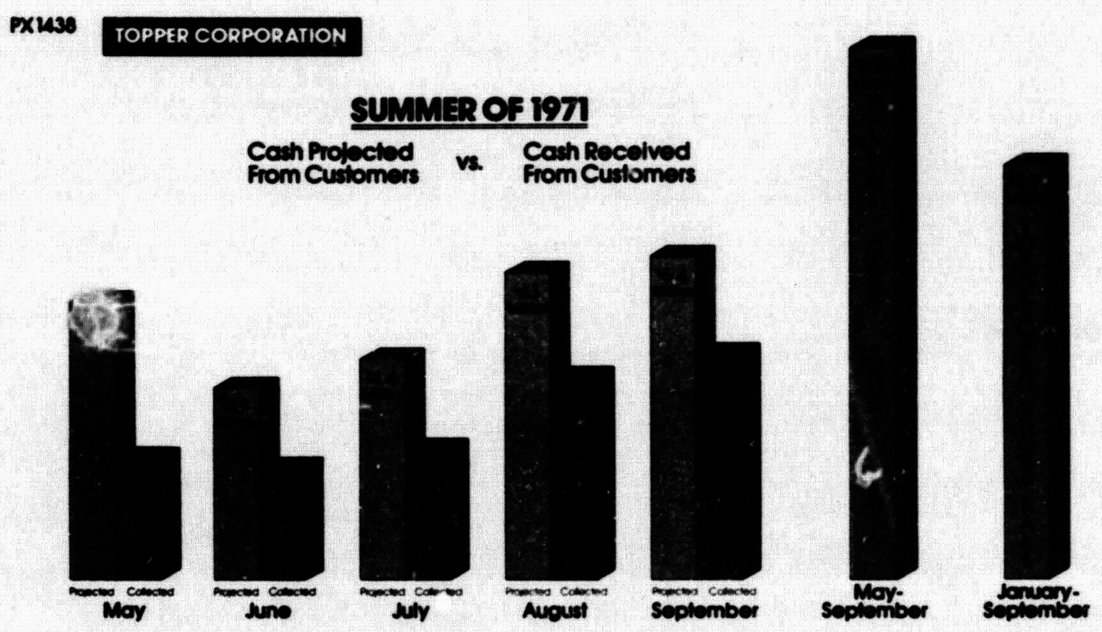
[92] An extended dating invoice listing run on May 20, 1971 showed that $13.7 million of the Spring 1971 Program receivables had not been paid (PX 348 at 26).



SOURCE: Topper Corporation Projection Analysis of Receivables and Inventory 1/1/71–1/31/72 included within Topper Corporation Preliminary Financial Statements as of December 31, 1970 and Projection of Operations for the Period Ending December 31, 1971 (PX 6, PX 393 and Citibank Admissions 65, 281 & 355) and the Loan Balance Pages of the Loan Status Worksheets for Jan.–Sept. 1971 (PX 333–341, PX 393, and Citibank Admissions 66, 294–302 & 355)

P177. It was thus clear "that Topper was experiencing a serious collection problem as of August 1971" (*Weiss Tr.* 795). "But the problems are pretty apparent here in May, June, July, when you are having significant short falls between projected and collected" (*id.*). As this Court observed, "In other words, anybody having that [information] in front of them wouldn't have made this $3,000,000 investment" (*id.*). Mr. Weiss of Price Waterhouse agreed, for the "effect of these poor collections . . . on the actual operations of [Topper]" represented "a serious problem at Topper Corporation with respect to that entity's viability as a going concern" (*Weiss Tr.* 835-36).

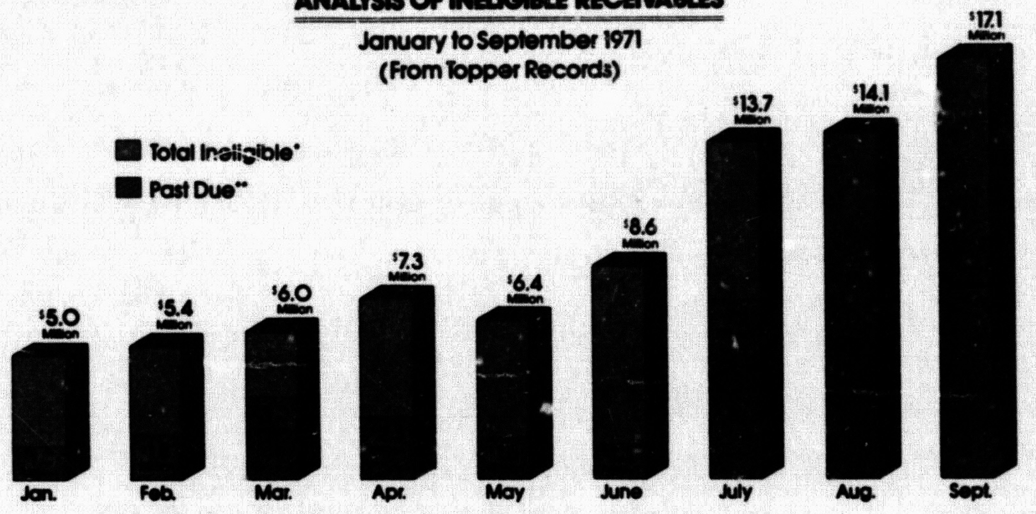
P178. Directly related to short fall in collections was the sharp increase in the amount of past due and ineligible receivables shown on Topper's own records, an increase which became particularly acute in the two months preceding the Private Placement:

TOPPER CORPORATION

PX 1439

ANALYSIS OF INELIGIBLE RECEIVABLES

January to September 1971
(From Topper Records)



*Accounts receivable that were listed as ineligible on materials submitted by Topper to Citibank. This includes receivables more than 60 days past due, except for redated receivables which Topper viewed as eligible throughout the period; the data excludes those receivables in January, February and March which were temporarily deemed ineligible because they were subject to a prior Letter of Credit issued by Manufacturers Hanover to finance the shipment of the underlying merchandise from the Orient; such receivables, which were subsequently deemed eligible upon arrival of the merchandise in the United States, are thus shown as eligible for the entire period.

**Accounts receivable that were past due more than 60 days according to Topper's records. This figure does not include approximately $2.2 million of redated receivables which were past due more than 60 days as of March 10, 1971 because they were viewed as "current" receivables by Topper management.

SOURCE: Topper Corp. Accounts Receivable Aging — Total Ineligible Receivables at Month End — Jan.-Sept. 1971 (PX 392 and Citibank Admissions 63 and 354)

P179. As striking as this data appears, it still fails to reflect the complete deterioration in Topper's receivables which took place. For example, the $14.1 million of past due and ineligible receivables shown for August are understated by more than $10 million; they fail to reflect:

(a) approximately $2.2 million in redated receivables originally due on January 10, 1971 and thus past due by more than 230 days (PX 1439 n. 2);

(b) roughly $5 million of New York Terminal Warehouse receivables stored in December 1970 which were subject to cancellation prior to shipment (PX 679);[93] and

(c) $3.1 million in customer credits, not payments, which had been applied to reduce past due receivables by mid-August (PX 1553).

P180. The sharp increase in past due receivables had real economic significance to Topper and was "a definite indication of a problem" (*Weiss Tr.* 808). According to the recently retired chief executive officer of James Talcott, Inc., a leading secured lender (*Slaughter Tr.* 1298-99), "past dues are always significant" because they affect "the financial condition of" a business (*id.* at 1311). This general concern over past due receivables is particularly heightened if:

> "the customers were not paying because the particular merchandise was not good and they were returning them and making claims. That would make you concerned not only about the financial condition of the client vis-a-vis the potential dilution, but also dilution in the receivables that are not past due yet as to

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[93] See Plaintiffs' Finding P76, *supra* at A79. Merchandise stored in the warehouse after March 10, 1971 was deemed ineligible (PX 679) and thus are reflected in PX 1439.

whether or not that merchandise was satisfactory" (*id.*).

P181. It was precisely because "the particular merchandise was not good" and customers " were returning them and making claims" (*id.*) that Topper's past due receivables jumped dramatically during the summer of 1971. Nor did this problem stem from the inability of Topper's customers to pay, since "most of Topper's customers were highly creditworthy" (*Weiss Tr.* 808), as Arthur Young had recently verified (*Cook Dep.* 108-09; PX 1011, 1012). Here the "problem" was clearly related to an oversold product line:

> "Usually you have a problem if you have a past due receivable because in Topper's particular situation, as I remember the depositions of Arthur Young, most of Topper's customers were highly creditworthy. So if they are having a significant problem in collecting receivables, the problem is usually at the store level—They are not selling the merchandise. That is an assumption that one can fairly make based upon the flow of the industry.
>
> "So if we have these past due receivables, basically it indicates at the store level a particular problem that customers are having in selling the particular product" (*Weiss Tr.* 808).

P182. Confirming that the receivable problem was directly related to the failure of Topper merchandise to sell at retail was the lack of any significant movement of toys stored in the New York Terminal Warehouse. Thus Topper, which initially anticipated that customers would "remove all such merchandise no later than September 1, 1971" (PX 484),[94] found that by August 31, 1971, roughly 85%

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[94] See, *e.g.*, PX 470, 471, 473, 474, 475, 476, 478, 479, 479A, 480, 481, 482, 483, 485, 486.

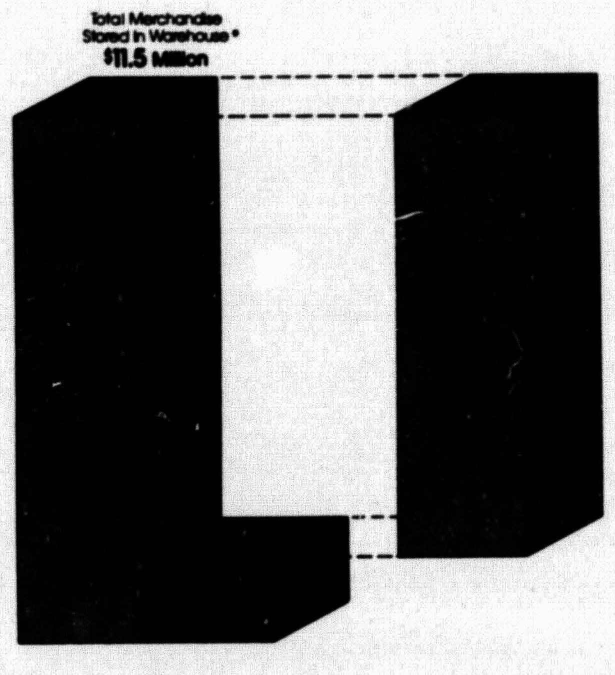
of the $11.5 million in merchandise stored there under the Spring 1971 Program and in 1971 remained unshipped:

PX1437

TOPPER CORPORATION

WAREHOUSE PROGRAM

At August 31, 1971



* Merchandise stored by Topper in the New York Terminal and Woodbridge Warehouses under the Spring 1971 Program and during 1971

SOURCE: Topper Corporation Terminal Whse. Recap 8/31/71 (PX 1001 and Citibank Admissions 179 & 933)

P183. Since the sharp rise in the past due receivables was plainly attributable to a faltering product line, equally fundamental questions were then raised concerning the worth of Topper's current receivables:

> "If the past due receivables are because your merchandise isn't moving on the shelves now, it is somehow a corollary to that that your current merchandise that you are trying to sell now probably might not move either.
>
> "As a matter of fact, the receivables aren't only problematic as far as being past due. Even current receivables are problematic because what you might have here is an indication of backup at the store level.
>
> "So there is not only a question as to collectibility of past due receivables, there is a question as to collectibility of the entire line of goods" (*Weiss Tr.* 810).

P184. The impact of this substantial deterioration in receivables on Topper's balance sheet was unmistakable. According to Mr. Weiss of Price Waterhouse "as of August 1971, Topper was experiencing a serious financial problem with respect to a principal asset, namely, its accounts receivable" (*Weiss Tr.* 802), a problem that seriously impacted its net worth:

> "Q. And the serious problem, again, Mr. Weiss, went to the assets of Topper Corporation?
>
> "A. Yes, went to the assets of Topper Corporation, and really, in reality, right down to the net worth of Topper Corporation.
>
> "Q. Why do you say it went to the net worth of the company?
>
> "A. Well, eventually what one has to consider is not only receivables, but if you can't collect them you are

> going to have to take a loss on them. If you take a loss on them, it is a direct charge or direct expense, and therefore a reduction of net worth, and can have a very serious effect on the net worth of the company if those receivables are not ultimately collected" (*Weiss Tr.* 803).

P185. Beyond a balance sheet effect, Topper's failure to collect its Dawn receivables, and the related failure of customers to withdraw Dawn merchandise from the New York Terminal Warehouse as anticipated, established that Dawn was not the non-seasonal item Topper had planned. As Mr. Weiss of Price Waterhouse observed:

> "[I]t is not only collectability. Basically, what we see here is a partial result of the Spring Program in actuality. The Spring Program basically was designed because Topper believed that its product had universal appeal, non-seasonal appeal, and if it had non-seasonal appeal, one would expect that significant amounts of this merchandise would be shipped to the stores and sold to the ultimate consumer.
>
> "What this chart [PX 1437] tends to show is they have extreme difficulty, basically, in placing this merchandise with the ultimate consumer because the retail establishments never called for the merchandise. What this means as far as receivables were concerned is that . . . if they had not used the merchandise they usually did not pay for it" (*Weiss Tr.* 788-89).
>
> • • •
>
> "Q. As of August 31, 1971, and based upon the information set forth in this chart, can a conclusion be drawn with respect to the success or failure of Topper's Spring 1971 Program at this point?

> "A. Well, it seems at this point that the Spring Program is in serious trouble, that the expected total non-seasonality of the Dawn doll was not expected, that in essence and in reality that what they had expected in the spring didn't come forth, and that Dawn was in fact a seasonal doll, to be sold probably in the following Christmas season" (*id.* at 790).

P186. The failure of Dawn to sell during the first eight or nine months of 1971 as anticipated, and the resulting build-up of massive amounts of Dawn inventory,[66] in fact meant that these toys would have to be sold "in the following Christmas season" *(id.)*. But this fact alone had striking implications on Topper's operations for the balance of 1971: the failure of Topper customers to sell their Dawn inventory significantly limited their ability to purchase additional merchandise in the coming months and had a corresponding limitation on Topper's ability to log additional sales in 1971. A principle example was the warehouse situation:

> "Q. Apart from collectibility, does the information on Plaintiffs' Exhibit 1437 relating to the warehouse program have any meaning with respect to Topper's ability to sell merchandise in the four remaining months of 1971, the period September through December?

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[66] In the twelve month period ending August 31, 1971 alone, Topper had shipped close to $50 million in Dawn dolls and accessories, (cf., CB ADM 56, PX 1168, PX 4) which accounted for roughly 80% (PX 718) of the $30.3 million in outstanding receivables shown on the August 31, 1971 balance sheet (PX 4 at 1). Between its introduction in April 1970 and the time of the Private Placement Topper shipped $61.3 million of Dawn merchandise (cf., PX 1069 & PX 5).

> "A. Well, again, the idea of the Spring Program was to move certain merchandise during the spring season and it was contemplated that this would be in addition to any sales that would take place subsequent to the so-called spring season. If they did not sell the merchandise within the normal spring season, then this merchandise would have to flow over and actually be in competition with Topper's own merchandise for the ensuing winter season.
>
> "So in other words, Topper was starting to face a crunch whereby it started to look like it had too much merchandise on the market.
>
> "Q. So that whatever the demand for Topper's products might be in the period September through December, in terms of their sales to meet that demand, the $9.7 million would be a reduction against it?
>
> "A. Well, they would certainly have to scramble a lot to make up for the $9.7 million" (*id.* at 790-91).

P187. Confirming the [e]ffect which the increase in unsold Dawn inventories had on Topper's ability to book further sales in 1971 was the significant decline in customer orders. Thus at the end of July there was a decrease of more than $7.5 million in customer orders from 1970, a period which itself saw a pronounced shortfall in sales and which, in significant part, was responsible for the deterioration in 1971.[96] The decline in orders continued during the first two weeks of August when another $1.4 million in orders were cancelled (PX 1223), as an

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[96] See Plaintiffs' Findings P114 - P125, *supra* at A97-A104.

August 18, 1971 Topper memorandum (PX 1223) makes clear:

> "J. Schwartz: 8/18/71
>
> You might find the following figures interesting
>
> | | *1970* | *1971* |
> |---|---|---|
> | Orders Booked thru 7/31 | $60,574,076 | $53,020,405 |
> | Orders Shipped thru 7/31 | 24,842,621 | 24,704,242 |
>
> August figures for 1971 do not look encouraging.
>
> Value of orders booked has decreased from the 7/31 figure to $52,553,569 as of 8/17/71. This decrease was caused in part by the cancellation of a stock control order of Pensick & Gordon for $515,802 and the adjustment of the stock control orders of Kresge, Lash & Grandway by $49,182 to offset retail and warehouse shipments.
>
> If we ship the $4.7 million that is planned for this month our shipments will be less than 1970 end of August."

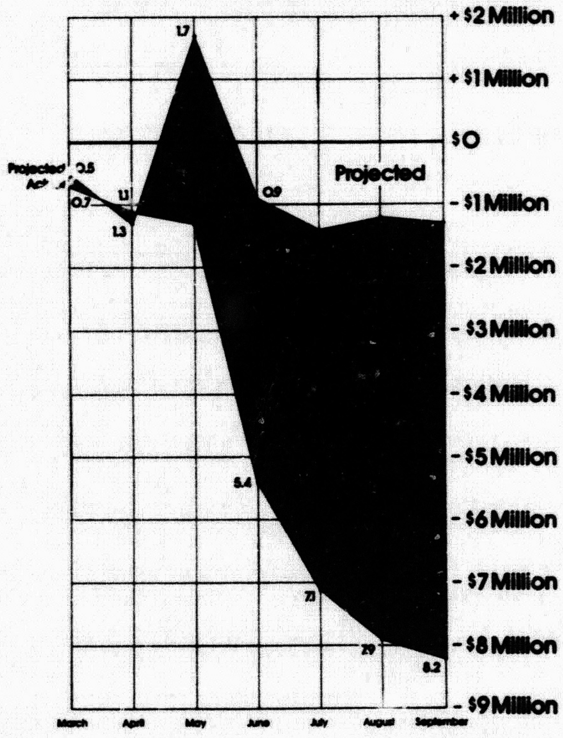
P188. However menacing these events were for the future, their impact on Topper's current operations in the summer of 1971 was equally dramatic. As a result of these financial difficulties, which "started in really significan[t] [terms] around May, when the extended dated sales became due" (*Weiss Tr.* 830), Topper was unable "to generate sufficient cash receipts to pay for its operations in the normal way that it should be expected that a corporation could do" (*id.* at 832-33). Reflecting what "the effect of these poor collections were on the actual operations of the company" (*id.* at 835) was Topper's actual cash flow from operations compared to projected cash flow:

PX1443

TOPPER CORPORATION

CASH FLOW FROM OPERATIONS
Projected vs. Actual*

(Cumulative from January 1, 1971)
For The Period March 1, 1971 to September 30, 1971



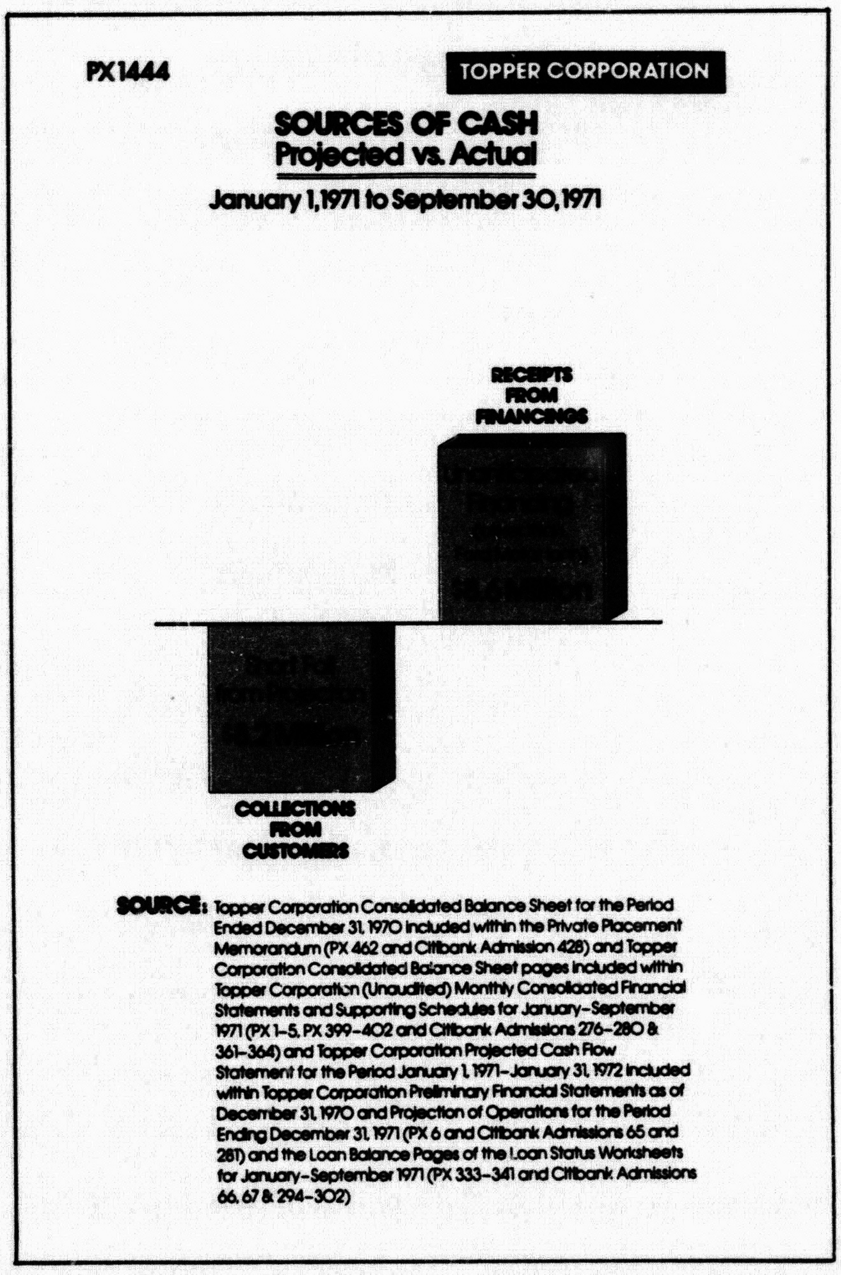
* Actual Cash Flow excluding Unanticipated Financings

SOURCE: Topper Corporation Consolidated Balance Sheet for the Period Ended December 31, 1970 included within the Private Placement Memorandum (PX 462 and Citibank Admission 428) and Topper Corporation Consolidated Balance Sheet pages included within Topper Corporation (Unaudited) Monthly Consolidated Financial Statements and Supporting Schedules for January–September 1971 (PX 1–5, PX 399–402 and Citibank Admissions 276–280 & 361–364) and Topper Corporation Projected Cash Flow Statement for the Period January 1, 1971–January 31, 1972 included within Topper Corporation Preliminary Financial Statements as of December 31, 1970 and Projection of Operations for the Period Ending December 31, 1971 (PX 6 and Citibank Admissions 65 and 281) and the Loan Balance Pages of the Loan Status Worksheets for January–September 1971 (PX 333–341 and Citibank Admissions 66, 67 & 294–302)

P189. By the end of August 1971 "there were definite problems evident" (*Weiss Tr.* 836) and Topper's prospects "were pretty bleak" (*id.* at 840). The "problem of receivables" was "having a ripple effect with the entire operation" (*id.* at 834) and "without some outside financing" Topper would not "have been able to continue as a going concern" (*id.* at 839-40):

> "Q Mr. Weiss, in your judgment, without the receipts from unanticipated financing during the summer of 1971, would Topper have been able to continue as a going concern?
>
> "A Topper would of course, as shown by the chart, have extreme problems meeting its projected disbursements goal, basically because of the problems of collectibility. Therefore, they would have extreme problems in meting its objectives without some outside financing. They definitely needed outside financing.
>
> "Q Their own operations then were not supporting themselves?
>
> "A No, they weren't supporting themselves, as can be seen here in the short fall.
>
> "Also, as you remember the previous charts, your Honor, they had a significant past due and ineligible percentage to total receivables. There was a significant problem as to whether those receivables would be collected and the prospects as of August 30th and September were pretty bleak."

P190. To meet these "evident" problems on a stopgap basis, Topper turned to outside financings to support its operations for the balance of 1971. As Mr. Weiss of Price Waterhouse put it, by the end of August, Topper was "just not generating the cash that they expected to generate, they still have a considerable amount of expected disbursements, but they can't meet them, and the difference, of course, is made up by the borrowings" (*Weiss Tr.* 834-35):



PX1444

TOPPER CORPORATION

SOURCES OF CASH
Projected vs. Actual

January 1,1971 to September 30,1971

SOURCE: Topper Corporation Consolidated Balance Sheet for the Period Ended December 31, 1970 included within the Private Placement Memorandum (PX 462 and Citibank Admission 428) and Topper Corporation Consolidated Balance Sheet pages included within Topper Corporation (Unaudited) Monthly Consolidated Financial Statements and Supporting Schedules for January–September 1971 (PX 1–5, PX 399–402 and Citibank Admissions 276–280 & 361–364) and Topper Corporation Projected Cash Flow Statement for the Period January 1, 1971–January 31, 1972 included within Topper Corporation Preliminary Financial Statements as of December 31, 1970 and Projection of Operations for the Period Ending December 31, 1971 (PX 6 and Citibank Admissions 65 and 281) and the Loan Balance Pages of the Loan Status Worksheets for January–September 1971 (PX 333–341 and Citibank Admissions 66, 67 & 294–302)

P191. Topper was thus able to continue through the summer of 1971 not by selling more toys or collecting more receivables, but instead by raising $15.6 million in unanticipated financings. Approximately $3.6 million of the unanticipated financings were raised in the spring public offering (*Weiss Tr.* 839) and $5,250,000 was raised in the Private Placement which closed on September 28, 1971 (CB ADM 1). The last $7 million came from the Ford Motor Credit Company on September 17, 1971 which agreed to assume a participation interest in the Finance Agreement, thus effectively reducing the exposure of the Citibank group (*Weiss Tr.* 838).[97]

P192. During the months of May through September 1971, the period so crucial to its 1971 operations,[98] Topper received roughly $15.5 million from its toy business (CB ADM 66) and more than $18.5 million from outside financings (CB ADM 67). The $18.6 million in outside financings raised by Topper during this period were remitted to Citibank in their entirety (CB ADM 89 & 90).

P193. Topper raised $5,250,000 of this outside capital by the sale of unsecured securities to plaintiffs. These securities were sold without the slightest disclosure of any of Topper's several and severe financial problems,[99] including principally:

(a) that its principal product, the Dawn line of dolls and accessories, had failed to sell at retail as anticipated and was currently being returned in substantial quantities;[100]

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[97] See Plaintiffs' Findings P291 - P292, *infra* at A179.

[98] See Plaintiffs' Findings P174 - P175, *supra* at A130.

[99] See Plaintiffs' Findings P8 - P20, *supra* at A48-A54.

(b) that as of August 31, 1971, almost $10 million in merchandise reported as sold was currently stored in a warehouse located on Topper's premises under terms comparable to the bill and hold practices which contributed to Topper's difficulties in 1965 and 1966;[101]

(c) that Topper was, and had been since May, in the midst of a serious cash flow problem, with customer collections falling short of projections by $10.5 million;[102]

(d) that Topper's principal asset, its accounts receivable, had deteriorated to the point where approximately 50% were now deemed unworthy for collateral by its own banker;[103]

(e) that as a result of these financial difficulties Topper was currently unable to generate sufficient cash to pay for operations and was presently experiencing a negative cash flow of more than $8 million;[104] and

(f) that Topper was only able to continue operations during the summer of 1971 as a result of a bridge loan which Citibank agreed to extend only on the condition that Topper consummate the Private Placement and remit its proceeds to the bank.[105]

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[100] See Plaintiffs' Findings P167 - P170, *supra* at A125-A127.

[101] See Plaintiffs' Finding P182, *supra* at A134-A135.

[102] See Plaintiffs' Findings P176 - P177, *supra* at A130-A132.

[103] See Plaintiffs' Finding P264, *infra* at A171.

[104] See Plaintiffs' Finding P188, *supra* at A140-A141.

[105] See Plaintiffs' Findings P271 - P272, P274 - P292, *infra* at A173-A179.

P194. Representations made by Topper concerning its financial condition were made in the face of a growing concern by its own finance department.[106] Indeed the failure of customers to pay their extended dating receivables, and the resultant cash shortfall of more than $10 million during the summer, was the subject of bi-weekly review at Topper beginning in mid-August 1971 and continuing through the Private Placement (PX 380-89; *Obolsky Dep.* 88; CB ADM 85-87). One such analysis, prepared on September 20, 1971 (PX 386), just eight days prior to the Private Placement, showed that 51 major customers who participated in the Spring 1971 Program had past due invoices of $16.9 million compared to $13.2 million in purchases under the Spring 1971 Program (see CB ADM 88).

P195. That Topper was in fact concerned about its receivable and collection problems prior to the Private Placement was subsequently acknowledged by Topper management at a December 20, 1971 meeting. Thus notes taken by a White & Case lawyer (*Provine Dep.* 320-24) reflect that in response to a question of when their concern first occurred, Orenstein and Rose both referred to the August and September period, citing the fact that collections were falling short in August and that the merchandise was still in the warehouse in September[107] (PX 1246 at 5).

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[106] See *Rose Dep.* at 414-19, 423-24, 434-35.

[107] This is consistent with the deposition testimony of Topper's chief financial officer, Mr. Rose; see *Rose Dep.* 414-19, 423-24, 434.

E.

Topper's Bankruptcy

P196. This concern proved warranted, for within two months of the Private Placement, on December 2, 1971, Topper announced that "sales and earnings of Topper Corporation for the current year 'will be quite disappointing'" (PX 600; CB ADM 190).

P197. Two weeks later, on December 17, 1971, Topper further announced that the $5 million profit projected to plaintiffs (PX 462, Exh. 3) prior to the Private Placement would instead be a significant loss (CB ADM 191; PX 601):

> "1971 has been an unexpectedly bad year for a number of companies which specialize in promotional television toys and recent developments are having a serious adverse effect on Topper's business. . . .
>
> "At this time last year Topper and its principal competitors engaged in sales programs providing for payments on extended terms, which in effect involved financing customers' inventories during a large part of 1971. New products in the low price range were specifically developed and produced for our program and we had high hopes for their success. So much so, that we misread actual market absorption early in the year and were led to produce and ship large additional quantities of similar merchandise to our customers during the first 9 months of 1971.
>
> ". . . More important, in spite of a relatively good movement of merchandise at retail, major retailers and distributors, faced with still large inventories and

> fearing a repeat of last year's disappointing Christmas, virtually eliminated all reorders of merchandise. . . .
>
> "As a result of these factors and of our being forced to accept returns from some overstocked customers and exchanges from others attempting to balance inventories, our operations for the year as a whole will result in a very substantial loss.
>
> "We believe that a major portion of our problems have their origin in last year's sales on extended terms . . . . $14,000,000 of last year's December sales was on extended terms. . . .
>
> "While we are unable now to determine the full extent of the loss, we believe, based upon information presently available, that it will be as much as $10-15 million, before effect is given to possible related tax benefits" (PX 601).

P198. In fact, the loss suffered by Topper in 1971 was far greater than even the $10 to $15 million loss announced on December 17, 1971. Though subsequent management[108] was "certain that a large segment of that loss should be more properly reflected in the 1970 financials" (*Clarke Dep.* 111), on "an arithmetic basis, such loss would amount to $37,232,000, the difference between the Company's consolidated earned surplus at December 31, 1970 of $2,749,000 and the consolidated deficit of $34,483,000 set forth in" Topper's consolidated balance sheet dated May 31, 1972 (PX 1101 at 3).

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[108] "Subsequent" or "new" management refers to the management group installed by the Board of Directors subsequent to February 1, 1972, including principally Mr. Henry Clarke, the chief executive officer; Mr. Roger Schlieder, the chief financial officer (*Schlieder Dep.* 8); and Mr. Ivan Samuels, an aide to Messrs. Clarke and Schlieder who conducted an extensive inquiry into Topper's prior difficulties (*Samuels Dep.* 10).

P199. After "one of the most comprehensive audits" made by Arthur Young and subsequent management (*Schlieder Dep.* 23), it was disclosed that "credits aggregating approximately $24,000,000 were provided against customer accounts subsequent to December 1, 1971 for returns, exchanges, allowances and uncollectible amounts" (PX 1101 at 2).

P200. During the month of December 1971 alone, approximately $19 million of credits were issued by Topper to its customers (CB ADM 195; PX 1098 at 3; *Schlieder Dep.* 39-40). Such December credits alone approximated two-thirds of the $29,077,290 in total receivables shown on the June 30, 1971 financial statements of Topper (PX 2 at 2), the last statements shown any plaintiff prior to the Private Placement.[109] Included in this sum were more than $6.3 million in credits issued against merchandise stored in the New York Terminal Warehouse (PX 1098 at 2, 6-7; CB ADM 199).

P201. Although Arthur Young and subsequent management were unable to attribute any specific amount of the $24 million in credits issued by Topper in late 1971 and early 1972 to the $14 million in Spring 1971 Program receivables reported in the 1970 financial statements, Orenstein himself acknowledged, on December 17, 1971, "that a major portion of our problems have their origin in last year's sales on extended terms" (PX 601 at 1). And new

---

[109] See Plaintiffs' Finding P10, *supra* at A49-A50.

management was "certain that a large segment of that loss should more properly be reflected in the 1970 financials", where the Spring 1971 Program was reported as sales, income and receivables (*Clarke Dep.* 111).

P202. By far the major portion of the $24 million in credits issued by Topper subsequent to December 1, 1971 was attributable to the return of non-defective merchandise which customers had been unable to distribute or sell at retail (PX 1098 at 2). Orenstein acknowledged that Topper's "very substantial loss" was attributable to "being forced to accept returns from some overstocked customers and exchanges from others attempting to balance inventories" (PX 601)—"there was just too much merchandise in the market and our business judgment was that we were forced to accept it to give [Topper] a chance to survive" (*Orenstein Dep.* 190).

P203. In point of fact, such "merchandise had been in the marketplace for considerably longer than the current marketing period and that some of the people who had received goods had a different view as to their commitment with regard to those goods than was stated" (*Clarke Dep.* 62).

P204. In any event, "[m]erchandise returns also contributed to the build-up of substantial carryover inventories of the 1971 Topper line. This buildup, together with the Company's liquidity problems, led management in 1972 to discontinue production of the Topper line pending disposal of such inventories" (PX 1101 at 3).

P205. According to an analysis prepared by Topper management on January 21, 1972 (PX 391) and forwarded to

Arthur Young on January 27, 1972 (PX 809), Topper issued credits of $12,174,618 for "returns," $2,560,986 for "markdowns", $2,458,579 for "advertising and rebate" allowances, and $4,698,657 for "miscellaneous" concessions (CB ADM 196).

P206. A more complete analysis put together by Topper management in 1972 in connection with their preparation of a balance sheet dated May 31, 1972, showed that subsequent to September 30, 1971 Topper issued credits of $18,269,363 for merchandise returns and $4,946,844 for "special allowances", most of which were applicable to the 1970 financials (*Clark*[*c*] *Dep.* 111-12; PX 870 at 2-3; CB ADM 197).

P207. On January 15, 1973, Arthur Young withdrew its certification of Topper's 1970 financial statements (CB ADM 201); because "certain information has come to our attention concerning the existence of a number of agreements made by Topper with its customers providing for rights of return, exchange and other concessions applicable to 1970 sales" (PX 867).

P208. On May 7, 1973, Edward J. Ryan, Referee in Bankruptcy, Southern District of New York, decreed "that TOPPER CORPORATION, be, and the same hereby is declared and adjudged bankrupt"[110] (CB ADM 202).

P209. The $4,250,000 of Topper Notes sold plaintiffs in the Private Placement are now worthless (CB ADM 203).

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[110] Order Adjudicating the Debtor a Bankrupt and Designating a Trustee, *In re Topper Corporation*, 73-B-203 (S.D.N.Y., May 7, 1973).

IV.

CITIBANK'S KNOWLEDGE OF TOPPER'S DIFFICULTIES AND ITS ROLE IN EFFECTING THE PRIVATE PLACEMENT

A.

Financial Information in the Possession of Citibank

P210. To enable effective administration of the Topper loan, Citibank representatives were in communication with Topper officials on a daily basis during 1971 (*Siegel Dep.* 114), and were advised during the course of such communications of each day's results. As Topper's Controller testified:

> "[I]n the normal course of business, it was not unusual to call the bank. And normally the contact at the bank was Mr. Morty Siegel. And calls were made either through me, Sandy Obolsky or some other designated person on the Topper financial staff, to advise him how much billing was going out for that day, how much credit memos were issued, what the available net receivables were, for the purpose of the bank advancing additional funds against those receivables prior to their receiving the paperwork. And the paperwork was sent by courier each day to the bank" (*Schwartz Dep.* 398).

P211. In addition to daily communications with Topper, Citibank received by courier from Topper a variety of detailed information on a daily and monthly basis, including

> (a) "*Unaudited Consolidated Financial Statement* and supporting schedules for each month showing the

amount of finished goods and work in process as of the last day of the month and the total accounts receivable of that day;"

(b) "*Sales Assignment Schedule* for each business day showing daily invoice totals, attached to which was a computerized invoice register itemizing and totaling the invoices by customer;"

(c) "*Account Statement* prepared monthly for each customer of Topper showing details of the customer's open debit or credit balance as of the last day of the month;"

(d) "*Credit Schedule* for each business day during which any credit was allowed a customer, showing the daily total of credits on merchandise returns and other items, attached to which was a computerized credit register itemizing and totailing the credits by customer and, in the case of merchandise returns, showing the number and the description of pieces returned;"

(e) "*Remittance Report* for each business day, accompanied by customers' checks and attached vouchers, if any, showing the daily total for amounts received from all customers and itemizing receipts by customer, invoice number, date of invoice and amount;"

(f) "*Invoices*, with bills of lading attached if shipment was involved, itemizing toys purchased, unit prices, gross sales prices, purchase agreement discounts, if any, net sales prices and shipping discounts, if any, which invoices are numbered and could be tied into a sales assignment schedule and invoice register prepared generally two to six days after the date on the invoices;"

(g) "*Credit Memos,* showing amounts of credit adjustments to accounts of customers, the number of pieces and description of toys, if any, which were involved in the credit transaction, sometimes stating the reason for the credit (e.g., advertising allowance, trade discount), which credit memos were numbered and could be tied into a credit schedule and credit register often prepared and dated approximately two to six days after the dates on the credit memos described therein;"

(h) "*Loan Status Report* for each business day, showing the effects of the total invoices, credit and remittances for the past business day on the balance of the loan to Topper, and the effect of Topper's computations of the value of eligible accounts receivable and other collateral upon the 'availability: [*sic*] to Topper of additional loan funds based upon the current loan balance and the applicable credit limits;"

(i) "*Accounts Receivable Detail Trial Balance,* prepared as of the last day of each month and ordinarily received by Citibank within 10 to 15 days thereafter, showing total accounts receivable and a breakdown of accounts receivable into current, 30-day, 60-day, 90-day and 'other' categories;" and

(j) "*Annual Audited Consolidated Financial Statements* and *Annual Reports* of Topper, and occasional projections of sales, collections and cash flow" (*Citibank Interr. Resp. I* at 21-23).

P212. To make sense out of this mass of data, and to afford ready oversight over the Topper account, Citibank programmed the data received from Topper each business day into a computer which in turn provided, among other things, daily loan "advance sheets" reflecting the "essential results of all daily records with regard to the Topper account" (*Siegel Dep.* 195), including the amount of past-due and ineligible receivables, collections received and credits issued each day, as well as the status of the loan balances in relation to the lending limits of the Finance Agreement (CB ADM 215-216; see PX 603-647).

P213. The purpose of the advance sheets, which were typically reviewed and initialed by Citibank officials each working day (*Siegel Dep.* 288-89) was to "determine what the collateral statuses were, to be a guide for what advances were to be made, and the mechanics in which advances were made" to Topper each day (*id.* at 193; see CB ADM 217).

P214. To enable participating banks under the Finance Agreement to stay abreast of the status of Topper's loan, Citibank conveniently summarized the financial data set forth on its internal advance sheets in Participation Statements sent to Manufacturers Hanover on a weekly basis (CB ADM 218), including each week during the months of June through September 1971 (PX 650-665).

B.

Citibank Control of Topper

(i) *Control Over Funds Available for Operations*

P215. Under the Finance Agreement Citibank had sole authority to determine the amount of funds the Banks would provide Topper for its business operations (CB ADM 20). Thus Topper was advanced funds based upon the amount of receivables which Citibank "at their discretion" deemed eligible for advances, net of applicable discounts, and less such reserves as Citibank deemed proper and necessary (PX 506 at 20). Citibank "controlled the formula" which determined the amount of advances and "could declare ineligible any receivable they wanted at any time" (*Rose Dep.* 619-20). This was acknowledged by a Citibank official who agreed that "the final determination was ours" (*Lusk Dep.* 30).

P216. Citibank exercised its authority under the Finance Agreement to deny Topper funds which it would otherwise be entitled by loan limits established under the Finance Agreement by declaring certain categories of receivables ineligible for advances or creating reserves for returns and other concessions.[111] At least nine separate categories of Topper receivables were deemed ineligible for advances during certain periods of 1971 (see *Citibank Interr. Resp. I* at ¶ 30), including, for example, the August portion of the Spring 1971 Program during January and February 1971 (*id.* at ¶ 30(a)(9)), as well as receivables related to merchandise stored in the New York Terminal Warehouse after March 10 (PX 679), and redated receivables (PX 689).

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[111] See Plaintiffs' Findings P101 - P105, *supra* at A90-A94.

(ii) *Control Over Topper's Need For, And Ability To Raise, Outside Capital*

P221. From the outset of its relationship with Topper, Citibank required Topper to raise additional and subordinate financing whenever it viewed its own collateral insufficient. The first such instance arose in early 1967. Although the October 4, 1966 Finance Agreement was initially scheduled to endure through January 31, 1968 (PX 506 at 28), in early 1967, as a result of Citibank's refusal to advance funds on certain assets, Topper requested Citibank to vary the lending formula to provide additional working capital (PX 511 at 1). Citibank, however, "refused to vary said formula except on the terms and conditions" required by Citibank (*id.* at 2). Foremost among the terms required by the Bank, as a condition to varying the lending formula, was that Orenstein personally invest $500,000 as a junior participant in the Finance Agreement (*id.*), on a basis below the security interest of Citibank's (PX 513).[112]

P222. Citibank exercised its authority over Topper's need for outside capital once more on December 28, 1967, when, as a condition precedent to advancing funds through 1968, Citibank required that Topper cause "Henry Orenstein and other parties satisfactory to the Banks to participate with the Banks in their financing agreement with" Topper (PX 512 at 1). As part of this arrangement, Citibank further required that the "participation shall aggregate not less than $1,560,000 and shall be junior to the interest of the Banks" (*id.* at 2). In addition to Orenstein, Topper raised additional funds from certain officers and clients of the investment banking firm of Hayden Stone, who, like Orenstein, were close to Topper (PX 513, 520, 521, 522).

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[112] The terms of these "junior participation agreements" generally provided the investor's interest "shall at all times be subordinate to the senior participations of the undersigned Banks" and that the investor was not "entitled to receive any sums . . . unless and until["] the Banks were ["]satisfied" (PX 513).

P223. This pattern of control over Topper's need for outside capital arose once more on January 29, 1969, when Citibank agreed to renew the Finance Agreement through 1969, "conditioned on the agreement of Henry Orenstein and Marrius Orenstein to continue their junior participation to the extent of $1,000,000" on a basis junior to Citibank's interest (PX 529 at 1). In this instance, again, Topper procured private capital required by Citibank from insiders, not third parties.

P224. The sole occasion when Citibank strayed from its policy of refusing to permit outside financings which affected the collateral was on September 17, 1971, eleven days prior to the Private Placement. On that occasion, Citibank, despite earlier expressions of displeasure,[113] agreed to amend the Finance Agreement to permit the Ford Motor Credit Company to advance $7 million to

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[113] According to Mr. Rose, Citibank initially was "not happy" with the Ford Motor loan because "this was the first instance where [its] collateral was being affected" (*Rose Dep.* 563). "The nature of the concern was the pressure that they had a tendency to build up on everything that they felt was appropriate for them, and if Mr. Waldman became upset he could increase that pressure, and that could be seriously harmful to us" (*Rose Dep.* 580).

Topper in order to reduce its outstanding share of the Topper loan (CB ADM 89).

P226. Citibank's influence over Topper's ability to raise outside funds also took the form of agreeing or not agreeing to advance funds to Topper in lieu of certain anticipated financings. An example of this exercise of authority occurred during the summer of 1971 with respect to the Private Placement,[114] however, there were other precedents as well.

P227. Citibank was first faced with a request to advance interim funds in lieu of a financing in early May 1970, a month or so prior to its initial public offering in June, when Topper approached the bank "seeking a commitment from us in case their offering is not available by June, of an additional $3.25 Million" loan (CBX 30 at 1). While Citibank recognized that if the offering did "go through as planned" the matter would be "academic" (*id.*), it nonetheless "concluded we could not justify an additional $3.25 Million in non-receivable loans for this client at this time based on collateral we have" (*id.* at 2); besides, Citibank observed, "stock offerings as a take out has had their problems" (*id.*). With the public offering in fact taking place as planned, Citibank was spared the decision of advancing or not advancing funds in 1970.

P228. The question of an interim loan, or over-advance, arose once more on April 15, 1971 roughly two weeks prior to the closing of the April 29, 1971 public offering.

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[114] See Plaintiffs' Findings P271 - P272, P274 - P288. *infra* at A173-A178

A Citibank memorandum on that occasion indicates that Citibank agreed to interim financing through the public offering but did so only with the understanding that its over-advance would "be recouped by April 30th either thru [*sic*] shipments and collections and/or proceeds of public offering" (PX 687).

(iii) *Authority to Require Compliance With Projections*

P232. It was Citibank's "practice in setting up a line of credit for this account, which we did annually, to have them submit projections as to what their cash needs would be and when they would need it and what collateral would be generated to secure it" (*Holzman Dep.* 28-29; see *Lusk Dep.* 25-27).

P233. Compliance with these projections was each year a further condition imposed by Citibank for advancing funds to Topper. Reflecting this requirement, a February 16, 1967 amendment to the Finance Agreement provided that Citibank's agreement to finance Topper through 1967 was "conditioned upon the substantial adherence by [Topper] to the projection, dated January 11, 1967, of sales and expenditures for the year 1967" (PX 511 at ¶ 9). A comparable requirement was likewise incorporated in at least three other amendments to the Finance Agreement,[115] and if Topper should fail to meet the submitted projections, Citibank in the words of Mr. Waldman, had the option to "[t]ell them to find another source" (*Waldman Dep.* 94-95).

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[115] See PX 512 at 5; PX 529 at 1; PX 535 at 1.

(iv) *Citibank's Influence Over Topper's Sales Policies*

P235. In March, 1971 Citibank cautioned Topper not to "make commitments for" an expanded warehouse program "or any other new sales program" without providing Citibank "full details for our review and decision" (PX 683). When Topper failed to abide by the directions of Citibank, warehouse shipments were declared ineligible for advances.[116]

P237. On at least one occasion, Citibank conditioned "the availability of funds under said credit line" (PX 529 at 1) on Topper's achieving a specified amount of shipments and orders (*id.;* see PX 740 at ¶2). If Topper should fail to meet the sales levels specified, Citibank was further authorized to either require that Topper raise additional financing or, failing that, limited the amount of advances based upon certain collateral to a specified sum (*id.*).

P238. Citibank insisted that Topper "notify the Banks promptly of all such returns" proffered by customers (PX 506 at 25). And Topper was not permitted "without the prior written consent of" Citibank to "grant any credit, allowance or rebate, or accept returns of merchandise from any account debtor, which would materially or substantially affect adversely the collateral value of the Receivables assigned to" Citibank (*id.*). In addition, Citibank retained the express authority to notify Topper at any time "in writing", that thereafter "no credits, allowances, rebates or returns may be granted or accepted without the prior written consent of the Banks, in which event [Topper] from and after the time of receiving of such notice shall comply therewith" (*id.*).

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[116] See Plaintiffs' Findings P102 - P105, *supra* at A91-A94.

C.

Citibank's Knowledge of Topper's Substantial Difficulties During 1971

(i) *Lending Plans For 1971*

P239. As 1971 began Citibank required,[117] and Topper submitted, a projected statement of operations for the period ending December 31, 1971, including a cash flow projection by month (PX 6; *Siegel Dep.* 172-73). These projections indicated that as of that time Topper planned only one outside financing to support toy operations for the coming year.[118]

P240. Within a month of its January 21, 1971 projections, Citibank was informed by Topper officials that in addition to the public offering set for May, which had been expanded to raise $5 million instead of the original $3 million, Topper was planning a second financing of $5 million from an institutional investor.[119]

P241. On the same day it learned that Topper was planning to raise $10 million in outside financing in 1971, on February 23, 1971, Citibank agreed "to continue financing Topper Corporation for the year ending January 31, 1972 subject to the terms and conditions set forth in the Financing Agreement" (PX 539).

P242. That same day, the Citibank officers responsible for the Topper account initialed and approved a set of

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[117] See Plaintiffs' Findings P232 - P233, *supra* at A160.

[118] See Plaintiffs' Finding P161, *supra* at A122.

[119] See Plaintiffs' Finding P164, *supra* at A124.

"Advance Instructions" which set forth the limits of "Over-advance privileges" for the forthcoming year (PX 677). A Citibank official acknowledged that beginning in June 1971 Topper was not permitted an over-advance of more than $500,000 without the written approval of senior Citibank officials, principally Mr. Waldman (*Siegel Dep.* 349-50).

P243. "An over-advance is the amount of funds which have been advanced in excess of the percentage advance that you have agreed to make against receivables or inventory, as the case may be" (*Slaughter Tr.* 1320). "Over-advances [are] an unsecured loan, in effect" (*id.* at 1322) and thus "a matter of concern to a secured lender" (*id.* at 1321).

P244. The purpose of preparing advance instructions, a general practice among secured lenders (*Slaughter Tr.* 1320-21), is to enable the bank to determine, for any period of time during the year, the permissible extent that outstanding loans may exceed the value of present collateral *(id.).* An advance instruction "in effect sets forth the rate of advance against particular collateral" (*id.* at 1320), and is followed on a daily basis, typically by examination of computer runs. Advance instructions which "are exceeded by any substantial amount" are "a matter of concern to a secured lender" (*id.* at 1321).

P245. Although Citibank held a secured interest in all principal assets of Topper under the Finance Agreement, according to a Citibank Executive Committee report, Citibank advances in 1971 were based solely upon "eligible accounts receivable assigned with recourse" (PX 742), a fact confirmed by the 1971 advance instructions (PX 677). Even in those years when Citibank agreed to advance against non-receivable collateral, such advances would peak in March and April (PX 708 at 2; PX 667 at 2) and expire in July (PX 1555).

P246. Citibank stopped advancing funds against non-receivable collateral at the end of September 1970 (PX 1556; CBX 161 at 4). It was at this time that Topper, for all practical purposes, transferred its manufacturing operations to the Orient (see PX 709), where Dawn dolls and accessories were manufactured (*Lusk Tr.* 1092-93); as Citibank observed, this "low priced doll item, to be produced overseas . . . will not involve any additional plant investment" (PX 709 at 1). Inventory available for advances was likewise limited by the container shipment of Dawn merchandise directly to customers from the Orient.[120]

P249. When Topper remitted to Citibank on May 7, 1971 the entire $6.4 million in net proceeds from its public offering (CB ADM 77), funds available for advances under the Finance Agreement changed from an over-advance position of $4,405,339 on May 6, 1971 to an "availability" position of $1,435,920 on May 7, 1971 (CB ADM 219).

(ii) *Knowledge of Topper's $10 Million Shortfall in Collections During the Summer*

P250. While Topper had from time to time experienced collections shortfalls in the past,[121] prior to the end of

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[120] See Plaintiffs' Finding P149, *supra* at A115.

[121] According to Citibank's Mr. Lusk, Topper's "performance was generally spotty. Occasionally they were short, and on other occasions they exceeded the projections" (*Lusk Tr.* 1031).

1970 such shortfalls were generally insignificant, typically amounting to less than $500,000 (see PX 1559). In any event, the prior shortfalls were of limited duration (CBX 89 and 91), generally collaterialized by eligible receivables (CBX 91; PX 709) and recovered within a month (CBX 137, 138; see PX 1559).

P251. The first significant cash shortfall suffered by Topper occurred in May 1970 when collections for that month fell short of projections by $2.7 million (PX 1560). Significantly this initial shortfall was a direct result of the $2 million in December 1969 extended dating sales which fell due in May 1970 (PX 672 at 1; *Lusk Tr.* 1068). According to Citibank's Mr. Lusk, many of these same receivables remained unpaid by the fall of 1970 (*Lusk Tr.* 1068), a fact apparently confirmed by Topper's collection history for the remainder of the year (see PX 1560).[122] As a result of this collection shortfall, the amount of past due receivables increased from $1.2 million at July 1970 to $2.3 million at the end of August 1970 (PX 1440; *Lusk Tr.* 1069).

P253. Although Citibank was aware that collections were within projections at mid-April 1971 (PX 687), Citibank also knew that $16 million of extended dating receivables were coming due between May and August 1971 (PX 718). Within nine days after the $9.5 million in May 10 receivables fell due, Citibank compared actual collections to projections and found "that collections to date in May are approximately $1.4MM v.s. the $5.5MM projected for the month" (PX 688).

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[122] While collections basically kept abreast of projections in the four months following the May shortfall, payment of the 1969 extended dating receivables was apparently not realized in the last part of 1970, since Topper suffered a cash shortfall of more than $6.4 million for the final three months of the year (PX 1560). Confirming this, two of Topper's largest customers, Kresge and Korvettes, returned 50% of their 1969 purchases at the end of 1970 (see PX 967, 968, 969; see *Zoll Dep.* at 16-23).

P254. Citibank continued to follow Topper's cash collections as the summer of 1971 progressed, and was consequently aware of the more than $10 million cash shortfall which occurred during the critical months of May through September 1971 (*Waldman Tr.* 1245-46; see PX 1438). This shortfall was completely without precedent in the Topper account, exceeding even the $6 million shortfall which occurred during the last five months of 1970[123] and was substantially worse than the results at the end of August 1969, when collections were exceeding projections (PX 709 at 2) and August 1970, when collections year to date were within a $1 million or so of projections (PX 1560). According to Mr. Lusk of Citibank, never once during the four year period 1968 through 1971 was there a comparable "period when Topper had had a shortfall from projections of $10 million in cash" (*Lusk Tr.* 1107).

P255. Apart from information prepared by Topper and submitted to Citibank each day, a similar cash shortfall was evident from information shown on a Citibank computer printout. Thus for the months of May through September, actual collections shown on the daily advance sheets compared with projected collections as follows (000 omitted):

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[123] See Plaintiffs' Finding P124, *supra* at A103.

1971 Month	*Actual Collections Shown on Citibank Advance Sheets*[124]	*Topper's Cash Flow Projections*[125]	*Collections as % of Projection*	*Cumulative Cash Shortfall*
May	$2,854	$5,495	52%	$2,641
June	2,476	3,775	66%	3,940
July	2,835	4,355	65%	5,460
August	4,292	6,115	70%	7,283
September	4,809	6,430	75%	8,904

P256. A direct consequence of Topper's collection difficulties during the summer of 1971 was a corresponding failure to pay its own bills when due. This fact too was well known to Citibank who was also aware that the reason for the increased payables was the fact "they simply don't have funds" (PX 702 at 4), as an August 8, 1971 Citibank audit report makes clear:

> "Aging of payables was done as at 6/30/71, most current available run, by invoice dates. Checks held totalling $1.7 MM paying June/71 and prior bills were also aged and added back to payables. Payables are delinquent in that $1.86 MM or 35% of the total outstanding of $4.904 MM aged, are past dues. The supervisor said that in most cases, checks are held for price disputes; however, the bookkeeper in charge of cash disbursements said they simply don't have funds" (*id.*).

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[124] See PX 645, 646, 647, 624, 644.

[125] See PX 6.

(iii) *Knowledge of the Substantial Deterioration in Receivables*

P257. Citibank was also aware of the significant increase in past due receivables, particularly the sharp rise which occurred between the end of June and the end of July 1971. In addition to receivable information reported by Topper showing an increase in past due receivables from $1.3 million at the end of June to $7.2 million at the end of July (PX 1439), Citibank's advance sheets reflected a 300% increase during this one month period. Thus Citibank's records "showed that the amount of Topper's receivables sixty-one days or more past due were approximately $3.5 million at mid-July 1971 and approximately $9.5 million at mid-August 1971" (CB ADM 223).

P258. Moreover, Citibank was well aware that this substantial increase from July to August 1971 was only a part of a trend that began in late spring 1970. Indeed by the end of August 1971 past due receivables were five times the amount outstanding for the comparable period in 1970 (PX 1440) and nearly fourteen times as great as in 1969 (CBX 161).[126]

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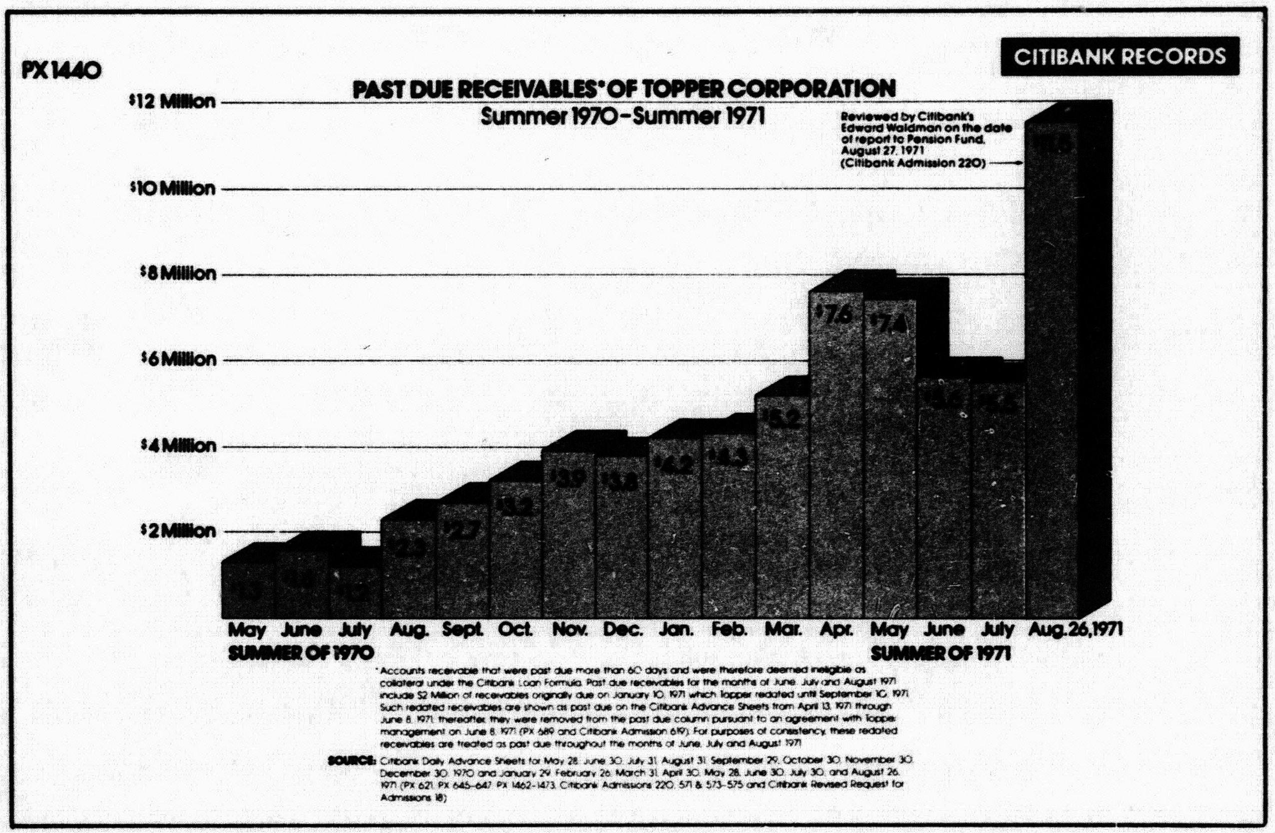
[126] Based on $690,956 in past due receivables as of July 25, 1969; there is no available data for August or most of September 1969 (CBX 161).



PX1440

CITIBANK RECORDS

PAST DUE RECEIVABLES* OF TOPPER CORPORATION
Summer 1970 - Summer 1971

Reviewed by Citibank's Edward Waldman on the date of report to Pension Fund, August 27, 1971 (Citibank Admission 220)

* Accounts receivable that were past due more than 60 days and were therefore deemed ineligible as collateral under the Citibank Loan Formula. Past due receivables for the months of June, July and August 1971 include $2 Million of receivables originally due on January 10, 1971 which Topper redated until September 10, 1971. Such redated receivables are shown as past due on the Citibank Advance Sheets from April 13, 1971 through June 8, 1971; thereafter they were removed from the past due column pursuant to an agreement with Topper management on June 8, 1971 (PX 689 and Citibank Admission 619). For purposes of consistency, these redated receivables are treated as past due throughout the months of June, July and August 1971.

SOURCE: Citibank Daily Advance Sheets for May 28, June 30, July 31, August 31, September 29, October 30, November 30, December 30, 1970 and January 29, February 26, March 31, April 30, May 28, June 30, July 30, and August 26, 1971 (PX 621, PX 645-647, PX 1462-1473, Citibank Admissions 220, 571 & 573-575 and Citibank Revised Request for Admissions 18)

P259. Citibank knew that the reason for the increase in past due receivables was the failure of Dawn merchandise to sell at retail (*Lusk Tr.* 1088; *Waldman Tr.* 1245), and not the inability of customers, who Citibank knew were "mostly well rated accounts" whose "bad debt experience is practically nil" (PX 671), to pay. According to Mr. Siegel, "there was very few in the way of Topper receivables that were not paid because of lack of funds" (*Siegel Tr.* 1174; see *Siegel SEC Tr.* 98-99). Confirming this, Citibank was informed during the course of a two day meeting with Topper officers on July 13 and 14, 1971 that Topper's "lagging" collections were the result of unsold inventories:

> "With regard to the discussions of collections, client advises that they are meeting some resistance by their distributors insofar as bills and invoices which are now due for payment, which customers claim that most of these goods have not been sold as yet" (PX 542).

P263. At the same time past due receivables were increasing at record levels in the summer of 1971, Citibank learned that a substantial and non-seasonal amount of credits were being issued by Topper for customer returns and other concessions (PX 1497 & 1498). Thus even though Citibank knew that credits were ordinarily not issued until "right around the Christmas season generally" (*Lusk Tr.* 1056), it also knew that the amount of credits issued for unsold Dawn merchandise in the spring and early summer of 1971 had more than doubled from prior levels (PX 702 at 3). In fact by the end of August 1971, Citibank advance sheets showed that more than $5.7 million in customer credits had been issued for returns and other concessions (PX 1497).[127] In terms of the significance of this data, Citibank's Mr. Lusk testified that credits amounting anywhere "from 20 to 50 percent would be substantial" (*Lusk Tr.* 1113). Pursuant to this test, the amount of outstanding credits issued by Topper by the summer of 1971 was "substantial" viewed against both collections and sales:

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[127] The $5.7 million in credits compared to $3.6 million of credits for the same period in 1970, an increase which occurred even though reported sales for the first eight months of 1971 declined by $3 million from sales reported in 1970 (PX 1497).

(a) credits for merchandise returns and concessions were more than 52% of Topper's collections from customers during May, approximately 50% of such collections in June, and in excess of customers' collections in July (cf., PX 1438 & 1498); and

(b) compared against sales, customer credits at the end of August 1971 amounted to 20.9% compared to 11.9% at the end of August (PX 1497).

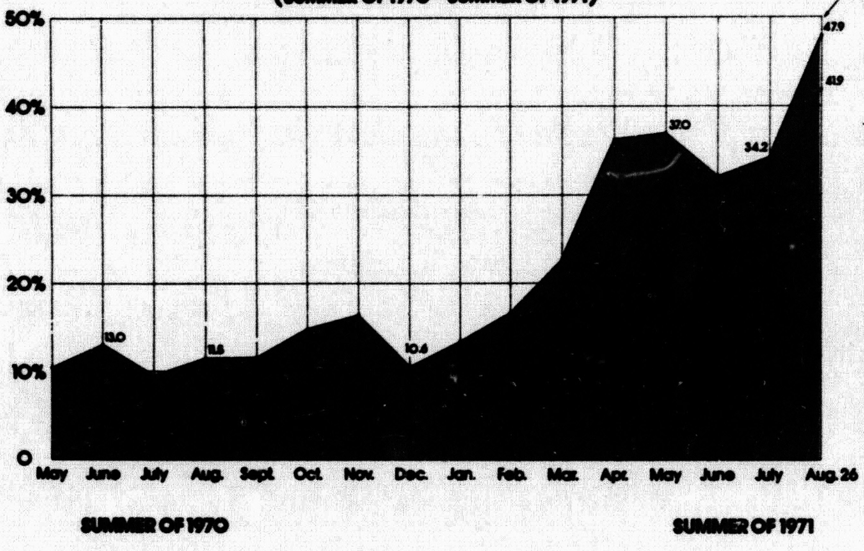
P264. The complete deterioration in Topper's business at the end of August 1971 was reflected most dramatically by the percent of Topper's past due receivables compared to all receivables over the 15 month period beginning with the summer of 1970 through the summer of 1971:

PX1441

CITIBANK RECORDS

PERCENT OF TOPPER CORPORATION RECEIVABLES DEEMED PAST DUE* OR INELIGIBLE BY CITIBANK**

(SUMMER OF 1970 – SUMMER OF 1971)



Reviewed by Citibank's Edward Waldman on the date of report to Pension Fund, August 27, 1971 (Citibank Admission 220)

* Accounts receivable that were past due more than 60 days and were therefore deemed ineligible as collateral under the Citibank Loan Formula. Past due receivables for the months of June, July and August 1971 include $2 Million of receivables originally due on January 10, 1971 which Topper redated until September 10, 1971. Such redated receivables are shown as past due on the Citibank Advance Sheets from April 13, 1971 through June 8, 1971; thereafter, they were removed from the past due column pursuant to an agreement with Topper management on June 8, 1971 (PX 689 and Citibank Admission 619). For purposes of consistency, these redated receivables are treated as past due throughout the months of June, July and August 1971.

** Accounts receivable that were deemed otherwise ineligible as collateral under the Citibank Loan Formula for reasons other than being past due more than 60 days. For purposes of consistency, two adjustments were made for December 1970 and January 1971. First, to correct for an understatement in the amount of gross receivables shown on the advance sheets, the amount of receivables attributable to the Drop Ship Program were restored to the gross receivable column on the advance sheets for the months of December 1970 and January, February and March 1971 (see "Response of Defendant First National City Bank to Interrogatories of the Hayden Stone Defendants, August 12, 1974, at ¶ 30(a)(5)"). This data was derived from the "Drop Ship" adjustment reflected on PX 392, a schedule prepared by Jack J. Rose, Topper's Financial Vice President (Citibank Admissions 68 & 364). Accordingly, gross receivables for the month of December 1970 include $10,789,000 in Drop Ship receivables; January 1971 includes $10,789,000; February 1971 includes $2,716,000; and March 1971 includes $1,413,000. Second, ineligible receivables attributable to the August portion of the Spring 1971 Program were removed from the ineligible column of the Citibank advance sheets for the months of December 1970 and January 1971 because they were subsequently deemed eligible for the months of February through August 1971, and thus do not appear as ineligible for the period (see response of Defendant First National City Bank to Interrogatories of the Hayden Stone Defendants, August 12, 1974, at ¶ 30(a)(9)). Accordingly, $2,034,000 in receivables attributable to the August portion of the Spring 1971 Program are not included as ineligible in December 1970 and $4,129,000 are not included as ineligible in January 1971.

SOURCE:
Citibank Daily Advance Sheets for May 28, June 30, July 31, August 31, September [illegible], October 30, November 30, December 30, 1970 and January 29, February 26, March 31, April 30, May 28, June 30, July 30, and August 26, 1971 (PX 621, PX 645–647, PX 1462–1475, Citibank Admissions 220, 571 & 573–575 and Citibank Revised Request for Admissions 18).

(iv) *Knowledge of Substantial Over-Advances Under the Finance Agreement*

P267. Citibank's lending plan for 1971 had called for over-advances during the period June through September of $500,000 or less (PX 677A).

P268. From May 7, 1971, when Citibank received the proceeds from Topper's public offering, to August 27, 1971, the day Mr. Waldman spoke to the Pension Fund, there was a negative swing of $6.5 million in the advance position under the Finance Agreement, from an availability figure of $1,435,920 on May 7 (CB REQ 18) to an over-advance of $5,052,302 on August 27 (*id.*).

P269. The adverse nature of the $5 million over-advance outstanding on August 27, 1971 is likewise clear. Thus an over-advance in the $1.2 million range on December 22, 1970 was described by Citibank as "a substantial over-advance" (PX 675). More significantly, the $5 million over-advance at the end of August was:

(a) 25% of the total loan outstanding on August 27, 1971 (see PX 622);

(b) $2 million more than was expected a month earlier at the mid-July conferences (see PX 542);

(c) $3 million more than was anticipated at the end of June (PX 541); and

(d) ten times the amount of permissible over-advances established under the Advance Instructions at the end of February 1971 (PX 677).

(v) *Citibank Agreed to Advance Additional Funds During the Summer of 1971 Conditioned on the Successful Completion of the Private Placement*

P271. Within a month of learning that collections under the Spring 1971 Program were falling substantially short of projections (PX 688), Citibank met with Topper officials on two occasions "to discuss certain collateral guidelines and the status of their account" (PX 689 & 541).

P272. During the first such meeting, on June 8, 1971, Citibank was informed by Topper management that it now planned three outside financings for 1971, rather than the one financing anticipated at the beginning of the year.[128] Thus, in addition to the April 29, 1971 public offering, the proceeds of which had been remitted to Citibank in early May (CB ADM 77), Topper was going ahead with two additional financings:

(a) a $7 million loan from the Ford Motor Credit Company, which was expected to close in late July (PX 689); as well as

(b) a $5 million private placement of Topper debentures, which they expected to sell by early August (PX 541).

P274. At a second meeting between Citibank officials and Topper management on June 21, 1971, Topper, in light of the growing shortfall collections (PX 1438) and in anticipation of the two forthcoming financings, sought Citibank's approval to go beyond the Advance Instructions set earlier in the year:

---

[128] See Plaintiffs' Finding P239, *supra* at A162.

> "Henry Orenstein advised me that Topper is currently negotiating with Ford Motor Credit for a loan of $7MM with repayment in 12 quarterly installments beginning on March 31, 1974.
>
> • • •
>
> "In addition the investment house is arranging for the sale by Topper of convertible debentures amounting to $5MM. They expect to receive the Ford money by July 25th and the debenture money by August 10th. Then Orenstein mentioned they needed $3MM over present availability through August 10th and we will be repaid out of the debenture money. I agreed to permit an overdraft of up to $2MM for this period of time" (PX 541).

P275. Citibank agreed to permit a $2 million over-advance in late June only on the condition that Topper successfully complete its outside financings and remit the proceeds to Citibank by early August 1971. As Mr. Waldman himself agreed, the $2 million over-advance was granted "on condition that the bank be repaid out of the debenture funds" (*Waldman Tr.* 1237).

P276. However, Topper's finances failed to improve in the two or three week period following the June 21 meeting (see PX 1438). As a result, the $2 million over-advance granted at that time was insufficient to meet Topper's growing operating deficit (see PX 1443).

P277. To review the extent of Topper's difficulties, and to map out a financial plan for the remainder of the year, a two-day meeting was held between Topper management and Citibank officials on July 13 and 14, 1971. According to Citibank, "[t]he purpose of this meeting was to bring us up to date on current happenings and at the same time make a request for interim additional advances" (PX 542 at 1).

P278. The first subject of discussion at this two-day meeting was the $7 million Ford Motor loan and the upcoming Private Placement. The proceeds of both financings were expected between August 10 and August 15, 1971. These funds, Topper management explained, would be turned over to Citibank to offset its current collection difficulties, which stemmed from the fact that distributors had been unable to sell the Dawn merchandise shipped in December under the Spring 1971 Program (PX 542).

P279. As a result of "lagging" collections, Topper management requested that Citibank grant additional over-advances to support Topper operations "as a bridge until the debenture funds and the Ford monies are received" (PX 542 at 2). Reflecting the salient points[129] of the July 13 and 14 meetings, Mr. Siegel of Citibank wrote on July 15:

> "With regard to the discussions of collections, client advises that they are meeting some resistance by their distributors insofar as bills and invoices which are now due for payment, which customers claim that most of these goods have not been sold as yet.
>
> "Along these lines, our records indicate as of June 30th that the following represents monies due which

---

[129] Orenstein testified that PX 542, the July 15, 1971 Citibank memorandum prepared by Mr. Siegel, did, to the best of his recollection, reflect the substance of the salient points discussed at the July 13 and 14 meetings with Citibank (*Orenstein Dep.* 168-69). See *Siegel Dep.* 110-11; *Waldman Dep.* 162.

> as yet have not been collected, 30 days, $800M, 60 days, $6,600M over 60 days, $3,500M.
>
> "In lieu of these slow collections, the additional expense of the new line, the client has requested that we provide some leaway in our present guideline as a bridge until the debenture funds and the Ford monies are received. We have agreed, therefore, to increase subject's line by $2½MM or a total of $21MM and provide for a $3MM over advance. This is without any advances against inventories and machinery and equipment. This over advance is an anticipation of an increase of the past dues which accur [*sic*] at the end of July together with advances to be made against the accounts receivable. But, in no event, should they exceed $3MM expected peak in the first week in August" (PX 542 at 2).

P280. Citibank, which at this point "welcomed" the Private Placement (*Rose Dep.* 77), agreed on July 15, 1971 to amend the Finance Agreement to increase temporarily the amount of permissible over-advances from the $2 million allowance granted in June to $3 million until August 15, 1971 (CB ADM 83; PX 543; see PX 541).

P281. Like the initial $2 million over-advance in late June, however, the $3 million over-advance granted on July 15 was conditioned upon the successful completion of the upcoming financings, and the remittance of those proceeds to Citibank. As Mr. Waldman of Citibank testified, Citibank "permitted the overdraft and increased the credit line on [the] condition that [we] receive the proceeds of" the Private Placement and the Ford Motor loan (*Waldman SEC Tr.* 63).

P282. Contrary to the plans mapped by Citibank and Topper at their mid-July meetings, the next six weeks or so failed to provide the financial improvement anticipated. Thus neither the Ford Motor loan nor the Private Placement closed in early August as planned (CB ADM 89 & 90) and, more significantly, Topper customers failed to pay any substantial portion of either the May 10 or August 10 receivables, as had been initially projected.[130]

P283. Reflecting the deterioration which began in May, and which failed to abate after the mid-July meetings, was the July 31, 1971 receivable report, delivered by special courier to Citibank on or about August 12, 1971. When the results of this report were entered, the amount of past due receivables shown on the advance sheets increased some 300%, from $3.5 million on August 12 to $9.5 million on August 13 (CB REQ 18).

P284. Despite the claim of Topper management that these receivables would in fact be collected, Citibank, acting under authority provided in the Finance Agreement, declared the receivables ineligible for further advances. As a result of this action, the loan availability under the Finance Agreement dropped sharply to an over-advance position in excess of $4.4 million (CB REQ 18).

P285. According to Mr. Rose, Citibank was "watching this and [was] . . . concerned about it, the collection problem" (*Thompson Tr.* 478; PX 1457). According to Siegel, "[i]n August, great pressure was put on [by] City Bank and Topper told customers to pay for the merchandise they had actually used" (PX 1551 at 4; *Skaar Tr.* 1356).

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[130] See Plaintiffs' Findings P158 - P160, *supra* at A121-A122.

P286. Although Citibank was in daily communication with Topper management during the months of August and September 1971 (*Siegel Dep.* 114), no further memoranda were written by Citibank officials relating to Topper's financial condition between the July 13 and 14 meeting and the Private Placement (*Siegel Tr.* 1147-48).

P287. Nonetheless, shortly after the anticipated increase in past receivables became the fact on August 12, 1971, management apparently met once again with Citibank officials to discuss Topper's financial difficulties and map out the steps required to see Topper through the Private Placement.

P288. At this mid-August meeting, an over-advance nearly twice as great as Citibank anticipated in late June was agreed upon (*Lusk Tr.* 1084-85). Evidencing the results of this meeting, on August 25, 1971, Citibank and Topper agreed to amend the Finance Agreement once more, this time to permit advances up to $4.8 million in excess of the eligible collateral (CB ADM 84; PX 547). According to Siegel, Citibank "went along at this time" because it knew the "debenture money" was coming in (PX 1551 at 4).

P289. At the end of August, Citibank recognized that Topper's collection and receivable problems had deteriorated more quickly than was anticipated even as late as mid-July. As one Citibank officer subsequently recounted to a Ford Motor officer: "Again the August collections were terrible. Gross receivables were approximately $35 million of which $17 million were past due and ineligible for one reason or another" (PX 1551 at 4).

P290. Nor was there any improvement in September 1971 as the amount of past due receivables reported by Topper to Citibank increased 37% from August (PX 1439) and collections fell short of projections by another $2.4 million (PX 1438).

P291. The Finance Agreement was amended once more prior to the Private Placement on September 17, 1971 (PX 1554). On this occasion, in a step which worked to reduce Citibank's financial commitment to Topper, Citibank agreed to share its first security interest under the Finance Agreement with Ford Motor Credit Company on a *pari passu* basis to the full extent of its $7 million loan.

P292. Despite expressing some displeasure at the proposed Ford loan early in June,[131] and even though Citibank "could have prohibited this loan by refusing to let" Ford Motor share in the collateral (*Waldman Tr.* 1220), by September 17, 1971 Citibank was "willing to enter into this Amendment in order to induce [Ford Motor] to make such loan" to Topper (PX 1554).[132]

P293. On September 28, 1971 the Private Placement was consummated as anticipated by Topper and Citibank on August 25, 1971 (CB ADM 1 & 227). The following day, on September 29, 1971, the $5,250,000 in proceeds of the

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[131] See Plaintiffs' Finding P224, *supra* at A158-A159.

[132] To further accommodate Ford Motor, Citibank acceded to their request that the $4.7 million in ineligible warehouse receivables (described as "Bill and Hold") be included within the collateral base as inventory (*id.* at 4). Ford wanted this "warehouse paper" deemed eligible in order to "comply with the ratios in the Ford agreement" (*Waldman Tr.* 1213). Citibank had "no objection, and the other banks didn't object, either, because we were not going to increase the loan balance at all" *(id.)*.

Private Placement were remitted to Citibank in their entirety (CB ADM 90).

P294. As a result of the Private Placement the Topper loan was again more than adequately secured by collateral —viz., from a $5 million over-advance on August 27, 1971, Citibank's record showed a cushion of almost $5 million in unused and eligible collateral on September 29, 1971 (CB ADM 219). Despite this substantial cushion, Citibank had no intention "to increase the loan balances at all" beyond this point (*Waldman Tr.* 1213).

P295. In the twelve day period from September 17 to September 29, 1971, Citibank's own share of the outstanding Topper loan was reduced by $5,282,862, from $8,524,034 on September 17 (PX 634, *Citibank Interr. Resp. II* at 5) to $3,241,172 on September 29 (PX 643; *Citibank Interr. Resp. II* at 5).

P296. The proceeds of this sale went to Citibank on September 29, 1971 (CB ADM 90). For its part Topper simply exchanged one form of debt for another: in place of secured debt bearing interest at the rate of 9% (PX 742) Topper substituted a debt instrument bearing 7.5% interest but "convertible at the option of the holder" (PX 462 at 1) into Topper common stock. For its part, Citibank was able to reduce the outstanding loan to Topper from $12,752,845 on September 28 (PX 642) to $7,717,076 on September 29 (PX 643).

V.

THE CITIBANK REPORT TO THE PENSION FUND ON AUGUST 27, 1971

A.

Citibank Fails to Disclose Any of the Finance Problems at Topper

P297. To verify the favorable report on Topper's financial condition received from management,[133] officers of the Pension Fund agreed in August 1971 that an independent inquiry "on the company's current financial condition at the moment" was appropriate (*Thompson Tr.* 427; *Inglis SEC Tr.* 85).

P299. Approaching Citibank in connection with the Private Placement, the Pension Fund wanted all material information relating to Topper's current financial condition that would be useful in evaluating whether to proceed with the purchase of Topper securities (*Thompson Tr.* 428-29), a fact which Citibank does not dispute (*Waldman Tr.* 1259). According to Mr. Mole, the Pension Fund

> "wanted to know from the bank . . . [which] was in a position to follow the company on a day-to-day basis, whether the company was in good financial condition as of that date, and whether the bank saw any clouds on the horizon" (*Mole Tr.* 670).

P303. Citibank's account manager for Topper, Mr. Siegel, believed he received and reviewed the prospectus prior to the April 29, 1971 public offering (*Siegel SEC Tr.*

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[133] See Plaintiffs' Findings P8 - P16, *supra* at A48-A52.

64-65; *Siegel Tr.* 1153-54); following such receipt, Siegel had a "general conversation" concerning the prospectus with the credit manager for Citibank's commercial finance and factoring division (*Siegel SEC Tr.* 65) and "remember[s]" thinking "this is a risky stock" (*id.*).

P305. Jeffers got in touch with Waldman and told him he received a call from Mr. Thompson of the United States Steel Pension Fund (PX 1505) concerning the Private Placement (*Waldman Tr.* 1257). Jeffers then asked Waldman to call Thompson (*id.*).

P306. In response to Mr. Jeffers' request Mr. Waldman, telephoned Mr. Thompson of the Pension Fund on the afternoon of August 27, 1971 (CB ADM 55).

P307. At the time he telephoned Mr. Thompson, Waldman knew that Thompson "represented the Pension Fund" (*Waldman Tr.* 1258-59); "the Pension Fund was considering purchase of the Topper debenture[s]" (*id.*); "the debentures were to be unsecured" (*id.* at 1253); there existed "a relationship on the part of U.S. Steel with the bank" (*id.* at 1258); and that Thompson "wanted all the information necessary" to evaluate the Private Placement (*id.* at 1254-55, 1259).

P315. With respect to the conversation Mr. Waldman testified as follows:

> "Q This is August 27th. Knowing Thompson's purpose and understanding what he wanted from you, did you tell him that Dawn, which was one of Topper's principal product lines, wasn't selling as anticipated? Did you tell Thompson that?

"A No, I didn't.

"Q Did you tell him that Topper's collections were lagging significantly below their projections?

"A No, I didn't.

"Q Did you tell him that Topper's receivables more than 60 days past due that day totalled $9 million?

"A No, I didn't.

"Q Did you tell him that Topper's receivables more than 60 days past due had tripled?

"A No, I didn't.

"Q Between August and June.

Did you tell him that the bank had agreed twice in the last five weeks prior to your conversation with Thompson to amend its financial agreement to permit over-advances?

"A Yes, I knew.

"Q Did you tell him that?

"A I didn't.

"Q Did you indicate to him that on the day of your conversation there was an over-advance by the bank almost amounting to $5 million?

"A No, I didn't." (*Waldman Tr.* 1259-60).

P316. Following this conversation with Mr. Waldman on the afternoon of August 27th, Thompson dictated a contemporaneous memorandum (PX 1379).[184]

---

[184] Mr. Thompson's memorandum, which was typed by his secretary the following Monday, August 30, states:

(a) "FNCB, as part of its lending functions, performs audits of Topper and Mr. Waldman said that this is one of the reasons his bank does not lend at a lower rate";

(b) These audits have shown "management . . . to be competent and to have good controls";

P317. Unlike Mr. Thompson, however, Mr. Waldman of Citibank prepared no memorandum on this conversation, contemporaneous or otherwise (*Waldman SEC Tr.* 27); and at least as late as 1973 Waldman had no "clear recollection of that conversation" with Mr. Thompson (*id.* at 44).

P319. Although Waldman and other officers testified that they had previously responded to various "credit checks" from various third parties,[135] he acknowledged that prior to the Thompson conversation on August 27, 1971, he had never been asked by Mr. Jeffers or any other senior bank officer outside his department to supply information concerning Topper or other accounts to a prospective investor (*id.* at 1256). Similarly, Mr. Siegel of Citibank testi-

---

(c) "The bank rates Topper above-average with respect to the other toy companies with whom it deals, and Mr. Waldman believes Jack Rose of Topper to be a very competent financial officer";

(d) "there are no problems at the moment nor does Mr. Waldman anticipate any" at Topper;

(e) "FNCB believes Mr. Orenstein to be extremely important on the marketing side of the business, but indicated that the company has done an excellent job of estimating cost of production for new toys. Mr. Waldman was aware that most of Topper's new items were developed by others than Mr. Orenstein and believes it is lessening its dependence upon him"; and

(f) "On balance, the bank thinks well of the company and that it rates highly among the managements of companies in the toy business. On the other hand, Mr. Waldman was unwilling to commit himself outright as to whether the toy business is one in which we should commit funds" (PX 1379).

[135] Citibank officers testified that from time to time they received "credit inquiries made to the bank concerning Topper" (*Lusk Tr.* 1014; *Siegel Tr.* 1130-31). These inquiries, according to Messrs. Lusk and Siegel, generally emanated from suppliers, such as "an automobile leasing company" who were apparently interested in in Topper's payable record (*Lusk Tr.* 1014).

fied that in all his years at the bank, no officer of Citibank from outside the Commercial Financial Division ever asked him to supply information concerning Topper to a client of the bank that was considering investment in Topper (*Siegel Tr.* 1152; *Lusk Tr.* 1083).

P320. Waldman subsequently indicated to two Citibank officers that he had given Thompson a favorable report during the course of their August 27, 1971 conversation. Thus Mr. Jeffers, the Citibank liaison officer who instructed Waldman to call Thompson (CB ADM 53 & 54), admitted that he subsequently learned Mr. Waldman "had given him a fairly favorable report" (*Jeffers SEC Tr.* 23-24). Likewise Waldman indicated to Morton Siegel, Citibank's account manager for Topper, that he gave Thompson a favorable opinion on Topper:

> "Q Right. I am interested in what Waldman indicated to you he told Thompson prior to the Private Placement.
>
> THE COURT: In other words, if you had gone home that night and your wife had said to you 'What do you think Waldman told Thompson', what would you have told her?
>
> THE WITNESS: That he gave a satisfactory reference.
>
> "Q A favorable opinion?
>
> "A I would say a favorable opinion.
>
> "Q So your impression from your conversation with Waldman was that he had given a favorable opinion on Topper to Thompson?
>
> "A That is my impression" (*Siegel Tr.* 1187-88).

P321. The fact of this favorable report was confirmed again when officials of the Pension Fund met with various Citibank officers on four separate occasions in the early part of 1972 (PX 1402; PX 1482; PX 1403; PX 1479). At no time during any one of the four meetings "did any Citibank official disagree with" the Pension Fund's "view that Waldman had given the Pension Fund a favorable report on Topper's financial condition" (*Mole Tr.* 695).

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

- - - - - - - - - - - - - - - - - - - -X

LESTER CONNELL, et al., :

Plaintiffs, :

-against- :

BERNSTEIN-MACAULAY, INC., et al., :

Defendants. : Consolidated Index
No. 72 Civ. 3272
(WK)

- - - - - - - - - - - - - - - - - - - -X

UNITED STATES STEEL AND CARNEGIE :
PENSION FUND, INC., et al.,
:
Plaintiffs,
:
-against-
:
HENRY ORENSTEIN, et al.,
:
Defendants.
:

- - - - - - - - - - - - - - - - - - - -X

FINDINGS OF FACT OF DEFENDANT FIRST NATIONAL CITY BANK ACCEPTED BY THE COURT

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DEFINITIONS AND ABBREVIATIONS

ADM -	Response of the Pension Fund, Connecticut Mutual and the Dallas Bank to Citibank's Revised Request for Admissions
ADM HS -	Response of the Pension Fund, Connecticut Mutual and the Dallas Bank to Hayden Stone's Revised Request for Admissions
Arthur Young -	Arthur Young & Company
AYX -	Exhibits marked at Arthur Young depostion testimony
Bagley -	Pat Bagley, Arthur Young
Belknap -	John Belknap, Arthur Young
Berlind -	Roger Berlind, Hayden Stone
Bernstein-Macaulay -	Bernstein-Macaulay, Inc.
Biondi -	Frank Biondi, Hayden Stone
Botte -	Salvatore Botte, Arthur Young
Byrnes -	Francis J. Byrnes, Hayden Stone
CBX -	Exhibits marked by Citibank
CIR -	Commercial, Industrial and Real Estate Financing Department, Ford Motor Credit
Citibank -	First National City Bank,
Clarke -	Henry Clarke, Topper
Connecticut Mutual -	Connecticut Mutual Life Insurance Company
CM Ans. to Interrog. (2nd Set) -	Connecticut Mutual's Answer to Citibank's Second Set of Interrogatories
CM Ans. to Supplementary Questions -	Connecticut Mutual's Answer to Citibank's Supplementary Questions to its Second Set of Interrogatories
Cook -	Errol Cook, Arthur Young
Dallas Bank -	National Bank of Commerce of Dallas (as Trustee of the Omega-Alpha, Inc. Pool Trust)
Dep. -	Deposition

Downs - David Downs, Topper

Finan - Walter Finan, Ford Motor Credit

Financing Agreement - Agreement between First National City Bank and Topper Corporation, dated October 4, 1966, as amended

Ford Motor Credit - Ford Motor Credit Company

Gray - John Gray, Dallas Bank

Harrison - Graham Harrison, Pension Fund

Hayden Stone - Hayden Stone, Inc.

Hieronymus - Leonard Hieronymus, Connecticut Mutual

Hinsey - Joseph Hinsey, White & Case

HSX - Exhibits marked by Hayden Stone

HS ADM PF - Response of Hayden Stone defendants to Revised Request for Admissions of the Pension Fund, Connecticut Mutual and the Dallas Bank

Hughes - Alexander Hughes, Topper

Inglis - Jay Inglis, Hayden Stone

Jaynes - Marvin Jaynes, Dallas Bank

Johnson - Glover Johnson, White & Case and director of Topper

Lang - William Lang, Pension Fund

Ledbetter - James Ledbetter, Bernstein-Macaulay

Lending Banks - The banks which at any time during the term of the Financing Agreement loaned or participated in the loan to Topper thereunder

Liell - Udo Liell, Arthur Young

Local 816 Fund - The Local 816 Labor and Management Pension Trust Fund

Local 816 Fund ADM -	Response of the Local 816 Fund to Citibank's Revised Request for Admissions
Local 816 Fund ADM (1st Set) -	Response of the Local 816 Fund to Citibank's First Set of Requests for Admissions
Lusk -	Albert Lusk, Citibank
McNally -	John McNally, White & Case
Manufacturers Hanover-	Manufacturers Hanover Trust Company
Mercantile -	Mercantile Bank of Canada
Molè -	Harvey Molè, Pension Fund
Morgan Guaranty -	Morgan Guaranty Trust Co., its predecessors and successors
Nelson -	George Nelson, Pension Fund
Obolsky -	Sanford Obolsky, Topper
Orenstein -	Henry Orenstein, Topper
Pension Fund -	United States Steel and Carnegie Pension Fund, Inc.
PF Ans. to HS Interrog. -	Pension Fund's Answer to Hayden Stone's Interrogatory
PF Ans. to Orenstein Interrog. -	Pension Fund's Answer to Orenstein's Interrogatory
Pierce -	Frederick C. Pierce, Topper
Pompea -	Ralph Pompea, Ford Motor Credit
Private Placement -	Topper Corporation private offering of $5 1/4 million of 7 1/2% convertible subordinated debentures dated September 28, 1971
Private Placement Memorandum -	Memorandum dated July, 1971 issued in connection with Private Placement
Provine -	John Provine, White & Case

PX -	Exhibits marked by the Pension Fund, Connecticut Mutual and the Dallas Bank
Ramseur -	Thomas Ramseur, White & Case
Rose -	Jack Rose, Topper
Samuels -	Ivan Samuels, Arthur Young
Schlieder -	Roger Schlieder, Topper
Schwartz -	Julius Schwartz, Topper
Siegel -	Morton Siegel, Citibank
Sterrett -	Conrad Sterrett, Hayden Stone
Thomas -	Bruce Thomas, Pension Fund
Thompson -	Henry Thompson, Pension Fund
Tinsley -	William Tinsley, Dallas Bank
Topper -	Topper Corporation
Tr. -	Trial Transcript
Van Deusen -	John Van Deusen, Pension Fund
Waldman -	Edward Waldman, Citibank
Walker -	Wilbert Walker, Pension Fund
Walsh -	John Walsh, Arthur Young
Weill -	Sanford I. Weill, Hayden Stone
Zoll -	Erle Zoll, Arthur Young

UNITED STATES DISTRICT COURT
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FINDINGS OF FACT OF DEFENDANT FIRST NATIONAL CITY BANK ACCEPTED BY THE COURT

Defendant First National City Bank ("Citibank") hereby submits the following Findings of Fact accepted by the Court in the above-captioned matter.

I. Topper and Citibank

D 1. Citibank and the other Lending Banks were parties to the Financing Agreement with Topper from late 1966 through 1971. Citibank acted as agent for the Lending Banks. (PX 506-519, 523-525, 529-532, 535-537, 539, 543, 546)

D 2. The Financing Agreement provided for a revolving secured loan by the Lending Banks to Topper. The loan was payable on a demand basis. Advances under the Financing Agreement were secured by all of Topper's assets, including accounts receivable, inventory, machinery and equipment and cash. (PX 506 at 2-8)

D 3. Under the Financing Agreement the Lending Banks were to make loans to Topper, at their discretion, up to 80 percent of Topper's accounts receivable which were determined by Citibank to be "eligible" for advances and against various other categories of Topper's assets. (PX 506 at 20)

D 4. Prior to 1971, the Lending Banks' advances from time to time included not only advances against Topper's eligible accounts receivable but specific advances against non-receivable collateral. The maximum amounts of any such non-receivable advances were called inventory or machinery and equipment "sub-limits". In 1971 the sub-limit categories were no longer used by Citibank in calculating the Lending Banks' advances, and the amount of advances was calculated solely by how it compared with 80 percent of Topper's eligible accounts receivable. (Lusk Tr., pp. 1017-1018)

D 5. During the period covered by the Financing Agreement Topper accounts receivable which were held "in-eligible" for advances at one time or another by Citibank included those accounts receivable which were past due more than 60 days, redated accounts receivable, accounts receivable due more than six months in the future, accounts receivable subject to a prior lien and accounts receivable on merchandise subject to certain warehousing arrangements between Topper and its customers. (Lusk Tr., pp. 1038, 1046-1047; PX 667, 675, 679, 680, 708; Waldman Tr., pp. 1211-1212; CBX 96, 103, 105)

D 6. The Financing Agreement at all times contained the following warranty to the Lending Banks by Topper:

> "(1) That each Receivable assigned hereunder for the purpose of the advance of funds . . . will be free and clear and will cover a bona fide sale and delivery of merchandise usually dealt in by it . . . ." (ADM 242; PX 506 at 11)

D 7. The Financing Agreement with Topper was administered by the Hubshman Factors Department (later the Factoring and Commercial Finance Department) of Citibank. This Department was formerly Hubshman Factors, Inc., which was acquired by Citibank in 1966. The Hubshman Factors Department was run in all material respects like an independent commercial finance company. (Siegel Tr., p. 1124; Silverman Tr., pp. 1290-1291) Aside from the lending-depository relationship, there were no other relationships between Citibank and Topper. Topper's checking account with Citibank was inactive, its active account being with Manufacturers Hanover. (Lusk Tr., p. 1020)

D 8. From 1966 through 1971 the Topper account with the Hubshman Factors Department was a "non-notification" accounts receivable financing arrangement, as opposed to a notification factoring arrangement. Under such non-notification arrangement Citibank had no right to deal directly with any of Topper's customers, and Topper itself made all collections from its customers and delivered them to Citibank pursuant to its assignment to Citibank of its accounts receivable. (Court Tr., p. 1401; Waldman Tr., pp. 1205-1206; Lusk Tr., pp. 1025-1026) Citibank's only contact during this period with Topper's customers was through confirmations sent out under the name of Henson Associates, Inc. (CBX 132-133) These confirmations were designed to appear as though they were from accountants reviewing Topper's books. (Lusk Tr., pp. 1025-1026)

D 9. Edward Waldman in 1971 was a vice-president in charge of the Hubshman Factors Department of Citibank. In such capacity, he had supervision over 150 accounts, of which Topper was the largest. Waldman spent approximately 5 percent of his time on the Topper account, meeting from time to time with Orenstein and discussing the account on a regular basis with Lusk and Siegel. (Waldman Tr., pp. 1206-1207)

D 10. Albert Lusk was account executive for the Topper account in the Hubshman Factors Department of Citibank for the period from 1968 through 1969. He spent about 10 percent of his time on the Topper account, which was his largest. In 1970 and 1971 he was credit supervisor over about 60 accounts, including Topper, and spent about 5 percent of his time on the Topper account. (Lusk Tr., pp. 1010-1012)

D 11. Morton Siegel became the account executive for the Topper account and about a dozen other accounts in early 1970, reporting to Lusk and Waldman. The time Siegel spent on the Topper account varied greatly on a daily basis. (Siegel Tr., pp. 1125-1126)

D 12. From the beginning of 1971 through September 17, 1971, advances under the Financing Agreement were made by Manufacturers Hanover (43%), Citibank (37%), Mercantile (5%) and Fidelity Union Trust Company (15%) as a participant in Citibank's advances. (Lusk Tr., p. 1015; PX 648)

D 13. On September 17, 1971, pursuant to an amendment of the Financing Agreement, Ford Motor Credit advanced $7 million to Topper. Ford Motor Credit's advances were secured, on an equal footing with those of the Lending Banks, by virtually all of Topper's assets. (HSX Ramseur 18; Siegel Tr., pp. 1136-1137)

D 14. Also on September 17, 1971, at the request of Citibank, Mercantile's five percent participation in the Finance Agreement, which amounted to more than $1 million of the more than $20 million outstanding (PX 1378), was terminated and assumed by Citibank. This termination was requested by Citibank because the income remaining to the Lending Banks when the Ford Motor Credit Loan to Topper went into effect was insufficient to be shared with Mercantile. (Siegel Tr., p. 1137; Lusk Tr., p. 1062; Waldman Tr., p. 1220)

D 15. During almost the entire period from 1966 through 1971, advances to Topper by the Lending Banks were substantially higher than 80 percent of Topper's eligible accounts receivable. It was normal for Topper to be in such an "overadvance" position. (CBX 161; Lusk Tr., pp. 1018-1019)

D 16. Overadvances to Topper existed during periods when Topper's sales and collections were under and above Topper's projections for such sales and collections. For instance, in April 1971, at a time when Topper sales and collections were both well ahead of projection, Citibank agreed to overadvances of $3.4 million. (PX 687; Lusk Tr., pp. 1075-1077)

D 17. The Financing Agreement and Citibank's administration of the Financing Agreement were typical and in accord with normal practice in the commercial financing industry. (Silverman Tr., pp. 1284-1285)

D 18. The relationship between Citibank and Topper was very similar to the other financing relationships in the Hubshman Factors Department and Citibank exercised no more or less control over the affairs of Topper than it did as to the affairs of its other factoring clients. (Lusk Tr., p. 1019) and no more than was normal in the commercial financing industry. (Silverman Tr., pp. 1286-1287) The only influence exerted by Citibank with respect to the affairs of Topper was its exercise of its right, as agent for the Lending Banks, to determine the amount of advances to Topper under the Financing Agreement. (Silverman Tr., pp. 1286-1287)

D 19. The documents which Citibank received from Topper relative to its loan, while more voluminous, did not differ from the documents received relative to other accounts.

Similarly, the documents created by Citibank relative to the Topper account did not differ from documents created for other accounts. (Lusk Tr., pp. 1023, 1027)

D 20. Citibank did not participate in or control Topper's various business or marketing practices, all of which were formulated and carried out by Topper itself. This was true of Topper's 1970 and 1971 extended dating programs (PX 667, PX 718), the redating of accounts receivable in 1970 (PX 667) and 1971 (PX 684), the warehousing of merchandise (CBX 103, 141), Topper's drop-ship program (CBX) 105) and Topper's practices as to returns, exchanges and other concessions (e.g., PX 675). Citibank discussed such practices with Topper solely from the standpoint of whether the Lending Banks would advance funds to Topper as to receivables involved in such decisions. Even when Citibank declared the respective receivables ineligible, Topper nonetheless pursued such practices. (CBX 103, 105, 141; PX 667, 675, 684, 718; Lusk Tr., pp. 1037-1039, 1041-1048, 1050-1056).

D 21. Examples of situations in which Citibank was advised by Topper after the fact with respect to certain of Topper's sales practices are reflected in the following exhibits:

(a) An August 28, 1969 memorandum of A. J. Lusk (PX 709) stated that:

> "Also for 1970, thru a wholly owned subsidiary of Topper, they are planning a line of Toiletries for the sub-teen market. A volume of $10MM is expected exclusive of the toy business. Distribution will be through some of the present toy outlets, i.e. Department Stores and Discount operations, as well as pharmacies and super market chains. Sales turnover is expected to be about 30 days which will tend to diminish the amount of capital required. Financing of this operation was not discussed."

(b) An October 31, 1969 memorandum of David L. Holzman (CBX 137) stated that problems in the production of Johnny Lightning cars for Topper by an outside company:

> "influenced the decision to set up his own production line which is now operating most efficiently. Since they expect to do $40MM in this item in 1969 and even more in 1970, they are happy to be in control of production."

(c) A January 19, 1970 memorandum of A. J. Lusk (PX 667) stated that:

> "Subsequent to the preparation of the above mentioned figures, the client learned that they would be obligated to re-date invoices for a substantial amount and so advised us. A major competitor initially offered very generous re-dating and Topper considers it good business to go along with customers requesting same. Approximately $2.5MM is involved in re-dating to 9/10/70 which covers the entire line of merchandise."

(d) A February 25, 1970 memorandum of M. Siegel (PX 669) stated that:

> "We received credits today in the amount of $731,662.57 representing customer rebates of 4% on volume purchases for 1969.

> According to Mr. Schwartz of Topper this rebate plan is offered each year to customers that buy over a specified amount by year end and rebate credit issued on 2/15."

(e) A July 16, 1970 memorandum of Morton J. Siegel (CBX 105) stated that:

> "Mr. David Downs was in our office on Wed. 7/15/70 and advised that Manufacturers Hanover had established a $5MM letter of credit and acceptance line which is separate and apart from their participation with us."

(f) A July 27, 1970 memorandum of Morton J. Siegel (PX 672) stated that:

> "Mr. Orenstein presented the new line which will concentrate more on non seasonal items and low cost merchandise."

(g) An October 30, 1970 memorandum of A. J. Lusk (PX 674) stated that returns were expected to run proportionately about the same as the year before (¶ 4). In addition, the memorandum stated that:

> "There will be some re-dating, but they do not expect that it will be in the proportions of the past year." (¶ 5)

(h) A December 18, 1970 memorandum of A. J. Lusk (PX 718) stated that Topper had started planning earlier that year:

> "to shift the emphasis from higher priced items ($10.) to the lower price range ($1-$2.)."

The memorandum also stated that:

> "to attract business for early 1971, they have been obliged to give special dating. Examples are Kresge ($2MM) and Korvette ($1MM) with terms due in May and August. . . ."

(i) A February 23, 1971 memorandum of A. J. Lusk (PX 678) stated that:

> "There is expected to be some redating of current receivables which Jack Rose will detail to us as soon as information is abailable [sic]."

(j) A March 24, 1971 memorandum of A. J. Lusk (PX 684) stated that:

> "In answer to my question of direct customer shipment, Jack said of the total first quarter shipments, he expects $500MM/$700MM to be shipped into New York Terminal Warehouse for customers under the usual arrangements.
>
> * * *
>
> "I also questioned Jack about the re-dating, - as the past dues seem to indicate the possibility of $3MM being re-dated. Jack said they are currently working this out with customers and although he did not have a firm figure, he estimates that re-dating will amount to somewhat more than last year's $2MM. They expect to have the details of this year's program within a few days."

(k) A March 26, 1971 memorandum of A. J. Lusk (PX 685) stated that:

> "Jack Rose advised as follows:
>
> 1. They hope to sign the contract for Sesame Street today. They have already developed the product but no tooling has been set up. He did not know the amount of tooling required. Shipments would not be forthcoming until the Fall months.
>
> * * *
>
> 3. The re-dating to September 10th is approximately $2.1MM. They will furnish for our review a schedule of the accounts involved and copies of the letters spelling out the terms. The accounts are mostly distributors."

D 22. In short, Citibank did not initiate or otherwise get involved with Topper's sales or marketing decisions. (Orenstein Dep., pp. 452-454; Lusk Tr., 1020) Citibank, in fact, had no contact whatsoever with Pierce, Topper's sales manager. (Pierce Dep., p. 148; ADM 262) Indeed, as one Topper officer put it, the banks did not presume to tell Topper how to run its business. (Downs SEC Dep., p. 12)

D 23. Citibank did not have or exercise control over Topper or its management or policies, directly or indirectly. The only control Citibank exercised was that control normally exercised by a commercial lender over its own funds.

D 24. Citibank in its handling of the Topper account observed proper, prudent and professional methods, all within the guidelines of proper, secured financing. (Silverman Tr., pp. 1284-1285)

II. Topper Financings

D 25. During the period from 1967 through 1971, Topper obtained funds from time to time through private placements from various individuals and institutions and through public offerings of securities. (Complaint, ¶20)

D 26. Topper was in bad financial condition at the time Orenstein acquired it from Philadelphia & Reading and it needed capital desperately. (Berlind Dep., p. 106) Its first acquisition of such capital was in late 1967-early 1968 when Topper sold $2,220,000 junior participations in the Lending Banks' loans through a private placement handled by Hayden Stone. (CBX 74; Weill Dep., p. 21) As it had done the year before when Henry Orenstein had a $500,000 junior participation (PX 511), Citibank conditioned its continuation of advances upon the junior participations (PX 512).

D 27. Three more Topper private placements, all arranged by Hayden Stone, took place between 1968 and 1970. (Weill Dep., pp. 31-36) The rights granted to the participants in such private placements were subordinate to the rights of the Lending Banks, which continued to have all of Topper's assets as collateral for their advances to Topper. (PX 506-519)

D 29. References to examples when Topper advised Citibank after the fact as to its financing plans are contained in the following exhibits:

(a) A January, 1968 memorandum of Michael J. Palermo (CBX 85) stated that:

> "To induce us to continue for 1968, principals have increased junior participation from $500M to $1,560,000. and have obtained cancellation of $19MM of debt (Extoy). Client has also obtained subordination of $8MM debt (Extoy) and extension of time for interest payments."

(b) A January 23, 1968 memorandum of David L. Holzman (CBX 134) stated that Topper:

> "Expects additional Junior participating money of 500M to 800M to be introduced some time before middle of March."

(c) A December 17, 1968 memorandum of A. J. Lusk (PX 708) stated that Topper's 1968 profits were net of:

> "$910M of interest in connection with the revamped Extoy (Philadelphia and Reading) debt. The recasting of the P & R debt provides for the forgiveness of $2.5MM of the original debt. The $2.5MM will be carried to net worth after the final payment in December 1969."

(d) An April 21, 1969 memorandum of A. J. Lusk (PX 743) stated that Topper was:

> "planning on a public issue of $3MM for year-end. Prospectus will be on a 8/31/69 statement, with entire proceeds for the benefit of the company."

(e) A May 15, 1969 memorandum of David L. Holzman (CBX 28) stated that because the production of Johnny Lightning cars by an outside company

> "falls below expectations, Topper has scheduled production lines to supplement [outsider's] production."

The memorandum also stated:

> "Because of the tight money situation in England, Lines Brothers has offered to give up its common stock holdings in Topper (10%) in exchange for redemption of its $1,000,000 of preferred stock. . . . To accomplish this, the stockholders intend to lend $1,000,000 to the company plus an additional $700,000 to provide in part the cash flow needed by Topper in view of the delays of shipments and increase in expenditures . . . ."

(f) A December 4, 1969 memorandum of A. J. Lusk (PX 710) stated that Topper was:

> "arranging to bring in $5MM of new subordinated money, of which they have $2MM '99%' committed. The latter will offset and they expect to prepay the subordinated note of $1,945M due January 15, 1970."

In addition, the memorandum stated that:

> "A stock bonus is an inducement for the subordinated lenders. They expect to make a public offering in late April for 300,000 shares at $10.00 per share for benefit of the Company."

(g) A May 8, 1970 memorandum of Morton J. Siegel (CBX 30) stated that the basis for a meeting of said date between Topper and Citibank:

> "was to discuss the possibility of their not being able to consumate a 3.8 Million dollar public stock offering which they had already budgeted."

(h) A June 8, 1971 memorandum from Morton J. Siegel (PX 689) stated that:

> "Mr. Rose advised that they expect some term financing, through Ford Motor Credit Co., in the amount of $7000M. A commitment is due in two-three weeks with receipt of funds expected within 30 days thereafter."

(i) A June 21, 1971 memorandum of Edward Waldman (PX 541) stated that:

> "Henry Orenstein advised me that Topper is currently negotiating with Ford Motor Credit for a loan of $7MM with repayment in 12 quarterly installments beginning on March 31, 1974. They have not yet worked out the specific amounts of the quarterly installments. Ford's rate is 5-1/2% above prime, but no greater than 14%, no less than 5-1/2% over prime.

* * *

> "Orenstein indicated they still felt that the term loan protected Topper in the event any of the present lenders should not renew at the end of the year. He apparently has been advised in this direction by Cogan, Berlind and Weil who have also handled his public offerings.
>
> "In addition the investment house is arranging for the sale by Topper of convertible debentures amounting to $5MM."

(j) A July 15, 1971 memorandum from Morton J. Siegel (PX 542) stated that:

> "According to the client, Ford Motor Credit has confirmed their $7MM term debt loan and will have the agreements ready by Monday, July 19th. The actual funds will be received approximately August 10th to 15th. These funds are to be given to us for which we will block the amounts involved and they participate with us in the collateral on a pari passu basis.
>
> * * *
>
> "The second subject the client discussed was the selling of $5MM to $7MM in 7 1/2% convertible debentures. We are advised that conversion price is $18. and the selling price as of July 13th is $16. We are advised further that Carter, Brelind & Weil, Inc. is selling these debentures to insurance companies and that by the end of the month the sale will be consummated and funds should be received by Topper approximately August 10th to 15th."

D 30. In June 1970 Topper had its first public offering of securities. This public offering, for which Hayden Stone was the lead underwriter, was for 440,000 shares of Topper common stock. (PX 554) No person at Citibank took any part in the preparation or distribution of any documentation relating to such offering or had any contact with Hayden Stone or Arthur Young, Topper's auditors, with respect to such offering. (Lusk Tr., p. 1060; Siegel Tr., p. 1135; Waldman Tr., pp. 1217-1218)

D 31. In April 1971, Topper had a second public offering of securities. This offering, for which Hayden Stone also acted as lead underwriter, resulted in the sale of 750,000 shares of Topper common stock. (PX 462, Exhibit 1)

D 32. As in the case of the 1970 Topper public offering, no Citibank representative took any part in the preparation or distribution of any documents relating to Topper's April 1971 public offering, or had any contact with Hayden Stone or Arthur Young relative to such offering. (Lusk Tr., p. 1060; Siegel Tr., pp. 1135-1136; Waldman Tr., pp. 1217-1218)

D 33. Citibank personnel were first advised in February 1971 of a possible Topper long-term loan. (CBX 35). This loan, which eventually became the Ford Motor Credit loan, was further discussed by Topper with Citibank in June, 1971. (PX 541) At that time, Citibank was advised that, subject to the bank's consent, Ford Motor Credit's advances under the loan were to be secured, on an equal footing with the Lending Banks' advances, by Topper's assets. (PX 541; Waldman Tr., p. 1218)

D 34. When advised that the Ford Motor Credit loan would decrease the amount of the Lending Banks' advances to Topper, while Citibank would still be required to do the same amount of work in administering such advances, Waldman expressed his disappointment (Rose Dep., p. 563) and demanded that Topper pay Citibank a service fee of one to two percent of Ford Motor Credit's advances to Topper. (PX 541; Siegel Tr., pp. 1136-1137; Waldman Tr., pp. 1218-1219; Lusk Tr., pp. 1061-1062) Citibank also terminated the participation of Mercantile because there was insufficient income to be shared once the Ford Motor Credit loan became effective. (Waldman Tr., pp. 1220-1221; Lusk Tr., p. 1062; Siegel Tr., p. 1137)

D 35. At the same time in June 1971 when Citibank was advised by Topper of the Ford Motor Credit loan negotiations, Topper told Citibank that it was preparing for the Private Placement. (Waldman Tr., p. 1221; PX 541)

D 36. The idea for the Private Placement originated with Topper, and was discussed with Hayden Stone in late 1970 or early 1971. (Orenstein Dep., pp. 145-146, 384-385, 388-389, 395-396; PX 1383). It was not discussed with Citibank, however, until June (PX 541) and later in July when Citibank was advised that it was to close in mid-August 1971. There was no further discussion between Citibank and Topper concerning the Private Placement until Citibank was advised at the end of September that Topper would be forwarding the proceeds to Citibank and that the "details of debentures and sale will follow". (PX 692)

D 37. Topper's reasons for having the Private Placement included (1) its desire for lower interest cost financing than was available under the Finance Agreement (PX 462, p. 5; Orenstein Dep., p.430); (2) its desire to ultimately replace its secured loans under the Finance Agreement with unsecured financing (Orenstein Dep. p. 428; Thompson Dep. p. 532); and (3) its need for more working capital to finance its anticipated expansion into the Sesame Street line of educational toys. (Ramseur Dep., p. 255; Waldman Tr., p. 1227)

D 38. Citibank did not tell Topper to have the Private Placement or insist that Topper do so. The idea for the Private Placement came from sources other than Citibank and Topper simply advised Citibank of its plans in that regard (PX 541; PX 1383; PX 1395). No representative of Citibank took part in the preparation or distribution of any documents relative to the Private Placement. No Citibank representative took part in any of the several Private Placement meetings between the purchasers, Hayden Stone and Topper. Similarly, no representative of Citibank saw the Private Placement Memorandum prior to the Private Placement. With the exception of Waldman, who saw only the subordination provisions of the Private Placement Purchase Agreement (Hinsey Dep., pp. 305-308), no Citibank representative saw such agreement prior to the Private Placement. In short, prior to the Private Placement, no Citibank employee had any knowledge about what information was given or not given by Hayden Stone, Topper or anyone else to any prospective purchaser in the Private Placement. (Lusk Tr., pp. 1062-1064; Siegel Tr., pp. 1139-1140; Waldman Tr., pp. 1221-1222)

D 39. Prior to the Private Placement, no one at Citibank knew or had reason to know whether anyone else had misled any plaintiff relative to its investment in the Private Placement.

D 40. Prior to the Private Placement, neither Lusk nor Siegel was aware that Waldman had had a phone conversation with Thompson of the Pension Fund, and neither Waldman, Lusk nor Siegel was aware that there was any custodial or other arrangement between Citibank and the Pension Fund, although Waldman assumed that the United States Steel Corporation was a large depositor of Citibank. (Lusk Tr., pp. 1063-1064; Siegel Tr., p. 1140; Waldman Tr., pp. 1222-1223; Thompson Dep., p. 467)

D 41. Prior to the Private Placement, no one at Citibank knew or had reason to know that any plaintiff was relying upon Citibank relative to its investment in Topper.

III. Topper in 1971

D 42. Prior to 1971, Topper's business fortunes were typical for a toy manufacturer. The toy business was highly speculative and seasonal. (Silverman Tr., p. 1281; CBX 163; PX 1028 at 2) Prior to Orenstein's repurchase in 1966 of Topper from Philadelphia & Reading, Topper had suffered very substantial losses, amounting in 1966 to more than $18 million. (CBX 162; ADM 1)

D 43. From 1966 through 1970, Topper's financial situation continued to fluctuate between good and bad times. It reported losses in 1967, some gains in 1968 and significant gains in 1969, but in 1970 its reported profits dropped 87 percent from their 1969 levels. (CBX 162; ADM 1). In early 1970, Topper introduced a line of children's cosmetics through a wholly-owned subsidiary, which incurred a loss of $876,164 and was discontinued in late 1970. (PX 462, Exhibit 1 at 7, Note (e))

D 44. The seasonality of Topper's business also continued, despite various efforts by Topper to stabilize sales on a year-round basis. (CBX 163-169; PX 708 at 2, 709, 710; CBX 137)

D 45. Topper's performance in meeting its projected collections was always sporadic, and its cash needs fluctuated considerably. (Lusk Tr., pp. 1030-1031, 1036) As Topper's projected collections failed to materialize, its accounts receivable would become past due, and Topper would require additional funds. (Lusk Tr., pp. 1032, 1035) Past due accounts, however, did not become bad debts but were eventually paid off. (Lusk Tr., p. 1035) Citibank personnel were not, moreover, overly concerned by Topper's erratic performance, as it was similar to what typically happened in such a business situation. (Lusk Tr., pp. 1036-1037)

D 46. From the standpoint of Citibank, the Topper account in 1971 was a good secured credit. Topper was regarded as a good company with good management. (Waldman Tr., p. 1224)

D 47. Topper had made profits over the last three or four years and had prospects for continuing that progress over the next several years. (Lusk Tr., p. 1064) The Lending Banks believed that they were adequately secured. (Lusk Tr., p.1064; Waldman Tr., p. 1224), In fact, as shown by CBX 160, which tabulates excess collateral over the loans outstanding during 1971 (Lusk Tr., p. 1016), the Lending Banks' collateral position appeared to be very strong during the Summer of 1971. In August 1971, for instance, the excess of collateral over loans was approximately $20 million. (CBX 160) Citibank had been advised by Topper that it was going to get the license to manufacture certain Sesame Street items, and felt that this would have a very substantial impact on Topper's sales and profits. (Lusk Tr. p. 1065; Waldman Tr., p. 1224) Topper's past securities offerings and its listing on the American Stock Exchange likewise had a favorable impact upon Citibank's consideration of Topper. (Lusk Tr., p. 1065-1066; Waldman Tr., p. 1224) Citibank personnel thought well of Orenstein's creative ability and Rose's financial capability. (Lusk Tr., p. 1066) In July 1971 Citibank had been advised by Orenstein that Topper had had the best six months in its history. (PX 542; Siegel Tr., pp. 1142-1143)

D 48. On the whole Topper's customers in 1971 were "of good quality" with respect to creditworthiness. As a result, Topper's bad debts in prior years had been relatively insignificant; and only one of Topper's accounts during the prior three years had gone into bankruptcy, on which account Topper had recovered more than 50% of the balance due. (HSX Ford 4, Schedule III, p. 2; Sterrett Dep., p. 88; PX 667 at 2, 671)

D 49. Topper's overall financial results during 1971, even before it began marketing its Sesame Street products, showed Topper to be in as good a shape as, if not better off than, prior years. Through June 1971, for instance, Topper reported a profit of $306,541 compared to a loss through June 1970 of $954,000 and through June 1969 of $194,000. The reported profit through July 1971 was $119,296 compared to a loss through July 1970 of $243,000 (CBX 163)

D 50. During the period from May through September 1971, Citibank was continuously aware of Topper's performance with respect to its May and August dating receivables, but was not overly concerned about this matter. (Waldman Tr., p. 1226) It was, after all, not normal experience that Topper have high sales prior to the latter part of the year. (CBX 169; Waldman Tr., pp. 1260-1262) Previous to 1971, Topper had not succeeded in overcoming the seasonality of its business. In late 1968, for example, Topper foresaw its Suzy Homemaker and Johnny Lightning toys providing a degree of stability as compared to the present surge of Christmas business (PX 708 at 2), yet 1969 remained as seasonal as ever (PX 744; CBX 137). Later, in August 1969, Topper predicted sales of Johnny Lightning toys alone of $9-10 million in the first quarter of 1970 (PX 709), only to revise this estimate significantly downward in October (CBX 137).

D 51. In addition, Topper's 1970 May dating, like its 1971 May dating, was not paid in May. Collections in May 1970, in fact, had been only 46 percent of projected collections for that month. (PX 717; Lusk Tr., pp. 1068-1069) Such 1970 May dating receivables, moreover, were not collected in the following two months, and they became past due at the end of July 1970 under the Financing Agreement's formula that accounts more than 60 days past due would be considered ineligible for advance.

(CBX 112; Lusk Tr., p. 1069) So when Citibank became aware in May 1971, as it had in 1970, that that year's May dating receivables were not being paid on time, it was hardly alarming. (PX 688; Lusk Tr., pp. 1069-1070) Similarly, when such receivables were not paid in the following two months and became past due receivables under the Financing Agreement formula at the end of July 1971, Citibank was not surprised. (PX 542; Lusk Tr., pp. 1070, 1102)

D 52. The amount of Topper's past-due accounts receivable on Citibank's books in August was not materially more significant than it had been previously in 1971. Citibank's advance sheets for such period (CBX 170) show the following percentages of past dues to total receivables:

January	21%	May	28%
February	19%	June	12%
March	19%	July	11%
April	29%	August	28%
		September	28%

These monthly fluctuations were not abnormal in the Topper account (Lusk Tr., pp. 1030-1032, 1035) and were no cause for undue concern. (Silverman Tr., pp. 1289-1290)

D 53. Similarly, the amount in July and August of Topper's total ineligible accounts receivable, which included past due receivables, was not materially more significant that in previous months in 1971. The corresponding percentages (CBX 171) on total ineligibles were as follows:

January	42%	May	37%
February	20%	June	25%
March	24%	July	28%
April	36%	August	42%
		September	29%

D 54. When the May 1971 receivables situation came to light in May, Lusk first discussed this matter with Rose. (Lusk Tr., p. 1070; PX 688) The matter was again discussed in the July meeting between Topper and Citibank. Accordingly, when approximately $6 million of Topper accounts receivable became past due in August, this event did not concern Citibank because it was foreseen and had already been discussed with Topper. (Lusk Tr., p. 1102)

D 55. In mid-July 1971 representatives from Citibank and Topper had a meeting to bring Citibank up to date and to request overadvances from the Lending Banks. Aside from advising Citibank that they had received a commitment from Ford Motor Credit to borrow $7 million from it and were planning to enter into the Private Placement, Orenstein discussed Topper's six-month earnings, Sesame Street, and the subjects of collections and overadvances. (PX 542; Lusk Tr., pp. 1071-1072)

D 56. Concerning Sesame Street, Orenstein advised Citibank that the line was being finalized and that sales, which he anticipated to be between $8 and $10 million, would start soon. Orenstein said that this new line of merchandise would afford Topper a tremendous advantage in selling its regular toy line, and enhance its ability to effect better collections, which recently had been lagging. (Lusk Tr., p. 1072)

D 57. With respect to collections, Topper indicated that some of its distributors had not been paying their bills because the merchandise had not been sold. Citibank's records showed that $3.5 million accounts receivable were more than 60 days past due, and that $6 million more would become past due if not paid by the end of July. (PX 542) Citibank suggested to Topper that it take a harder stance with its customers as to collections. Orenstein said that this would be the wrong approach at that time because of the effect upon the good will of the customers and because the impact of the Sesame Street line would give Topper a great deal of leverage with its customers. Orenstein preferred to effect collections more in accordance with Topper's normal seasonal patterns. (Lusk Tr., pp. 1072-1073) Orenstein said, however, that its collections could be effected right away if Citibank insisted that Topper take a hard line with its customers. (Lusk Tr., p. 1073; Waldman Tr., pp. 1225-1226) Citibank did not insist, but acquiesced in Orenstein's decision not to push for immediate payment by Topper's customers.

D 58. In the Summer of 1971, there was a severe credit crunch, during which many companies were investing all available funds instead of paying bills, and many other companies, consequently, were very hard pressed to effect collections. (Silverman Tr., p. 1283)

D 59. In short, there were no special problems with the Topper account in the period from May through September 1971 which were or which should have been cause for undue concern on the part of Citibank. (Silverman Tr., pp. 1289-1290)

D 60. Topper requested temporary additional overadvances in July 1971 because collections were down and because of increased expenses involved with the Sesame Street line. (Waldman Tr., pp. 1226-1227) Citibank agreed to increase temporarily the loan limit in the Topper account from $18.5 million to $21 million. This increased loan limit necessitated an amendment to the Financing Agreement for which the approval of the participant banks was required, and such approval was sought accordingly. (Waldman Tr., p. 1227) The increase in line, which was temporary, was extended in late August until the end of September. The additional overadvances included in these temporary increases in Topper's line of credit totalled approximately $5 million at one time in late August.

D 61. Topper's overadvances dropped from this amount to approximately $2 million prior to the receipt by Topper of the proceeds of the Private Placement. Upon reduction of the Lending Banks' loans with such proceeds, Topper had temporary availability of funds under the Finance Agreement of over $4 million. By mid-November Topper was again receiving overadvances of approximately $2.5 million. (CBX 161) Any repayment of advances they received from Topper as a result of the Private Placement, therefore, the Lending Banks gave back to Topper soon thereafter.

IV. Topper Business Practices and Knowledge of Them

Redating

D 62. In January 1970 Topper told Citibank that, in order to meet "generous redating" of a major competitor, it was going to redate to September approximately $2.5 million worth of merchandise. (PX 667; Lusk Tr., pp. 1044-1046) Redated receivables were receivables which were past due and for which the due date was changed to some future date. (Lusk Tr., p. 1039) Citibank initially established a reserve of $1.5 million against advances for such redated receivables. (CBX 96) In April 1970, however, when most of Topper's customers receiving redating confirmed their obligations with respect to such receivables, Citibank reinstated the redated receivables as eligible. (CBX 98; Lusk Tr., pp. 1046-1047)

D 63. In October 1970, Topper told Citibank that it expected some redating in 1971 but not as much as the previous year. Lusk instructed that Citibank take its normal conservative approach with respect to redating. (PX 674; Lusk Tr., p. 1048) In March 1971, while the Topper past due figures suggested to Lusk the possibility of $3 million being redated, Topper estimated that such redating would be slightly higher than the previous year's $2 million. (PX 684) Topper undertook once again to provide the documentation concerning redating, which actually amounted to $2.1 million. Topper's customers again confirmed the redated receivables. (Lusk Tr., p.1051) In April, Citibank advanced against redated receivables, then due in September, although it treated them as ineligible (PX 687), until in June 1971 Citibank made redated receivables eligible and advanced against them at the rate of fifty percent. (PX 689)

D 64. Prior to the Private Placement Topper's redating of certain accounts receivable from January 10, 1971 to September 10, 1971 was known to Hayden Stone (HS ADM PF 236), Arthur Young (ADM HS 204-205, 236; Weiss Tr., p. 848; PX 1067 (Tr., p. 744); Cook Dep., pp. 399-401), White & Case (HSX Ramseur 18; ADM HS 69, 72, 76-77; Hinsey Dep., pp. 50, 57-58, 263-267) and Ford Motor Credit (HSX Ford 4 (Schedule III, p. 1), 7, 10, 16; ADM HS 277, 290; ADM 214), as well as Citibank.

Warehousing (Bill and Hold)

D 65. During late 1970 and January 1971 some $5.8 million worth of merchandise which Topper had sold was shipped by Topper to a warehouse pursuant to a warehousing, or "bill and hold," arrangement between Topper and certain of its customers. Siegel, account executive of the Hubshman Factors Department for the Topper account, became aware of these warehoused goods in early 1971 when he returned from vacation and discovered that advances to Topper had already been made against such merchandise. (Lusk Tr., pp. 1051-1053; Waldman Tr. pp. 1209-1210)

D 66. As a result of conversations with Topper management, Citibank agreed to treat as eligible $5 million of the $5.8 million warehoused receivables against which the advances had been made. Citibank decided to treat any subsequent warehousing as ineligible pending further discussions with Topper and obtaining satisfactory documentation from Topper's customers relating to such goods. (Lusk Tr., pp. 1052-1053; CBX 103, 141; PX 679)

D 67. It was normal Citibank practice to treat warehoused, or "bill and hold", merchandise as eligible if Citibank received a confirmation to Citibank from the client's customer that it had taken title to the merchandise and that the other terms and conditions were as indicated. (Lusk Tr., pp. 1053-1054; Waldman Tr., p. 1210)

D 68. Waldman and Orenstein had discussions with respect to the subject of warehousing, and exchanged drafts of proposed documentation which each party wished Topper's customers to sign in connection with Topper's warehouse program. Orenstein refused to submit Citibank's version of a warehouse agreement to its customers because it would highlight the fact that Topper was financing by accounts receivable financing and Orenstein felt that this would embarrass him in his customers' eyes. Waldman, following Citibank's policy, would not make the warehoused receivables eligible for advance and such receivables were, accordingly, deemed ineligible. (Waldman Tr., pp. 1211-1212)

D 69. Under the terms of the Ford Motor Credit agreement with Topper, Topper was limited in the amount of loans it could receive from the Lending Banks. These loan limits were expressed as a percentage of eligible receivables. Ford Motor Credit and Topper requested that Citibank increase the amount of receivables which it deemed eligible so that the advances Topper received from the Lending Banks would not be above the limits set forth in the Ford agreement with Topper. Accordingly, in September 1971, at the time the Ford Motor Credit loan to Topper became effective, Citibank made the warehoused receivables eligible at the request of Ford Motor Credit and Topper at the rate of 50 percent of the cost of the merchandise. (Waldman Tr., pp. 1212-1214) This change in the treatment of such merchandise reduced the amount of the Lending Banks' overadvances but resulted in no more funds being advanced to Topper. (Waldman Tr., p. 1213)

D 70. Prior to the Private Placement Topper's practice of arranging for storage on premises leased by it of goods sold to certain customers was known to Berlind and Weill, officers and directors of Hayden Stone (HS ADM PF 240), to Hinsey and Provine of White & Case (ADM 214; ADM HS 60-61, 69, 72, 75; PX 497; Hinsey Dep., pp. 163, 255-258), and to Ford Motor Credit (HSX Ford 10; Pompea Dep., p. 260; ADM 214; ADM HS 270), as well as to Citibank.

D 71. During its 1970 audit of Topper Arthur Young also knew that as part of its 1971 Spring Program and as part of its normal sales program to certain customers Topper arranged for the warehousing on premises leased by it of goods sold to customers. (ADM HS 146-149, 151-152, 158, 163, 171; Weiss Tr.,p. 848)

D 72. During its cold comfort review of Topper for its April 29, 1971 public offering, Arthur Young was aware of the amount of goods shipped into and out of that warehouse during the first three months of 1971. (PX 997-1000; ADM HS 166-168)

D 73. During its 1971 audit work done in September 1971 Arthur Young also knew the amount of goods that had been shipped into and out of that warehouse as of August 31, 1971 and September 30, 1971. (PX 1001-1002)

D 74. During its 1970 audit Arthur Young reviewed Topper's contract with the New York Terminal Warehouse and the agreements between Topper's customers and that warehouse (ADM HS 158; Zoll Dep., pp. 43-44), employed special audit procedures with respect to 1971 Spring Program merchandise shipped or to be shipped into the New York Terminal Warehouse and insisted that a reserve of approximately $1.5 million be established based upon the profit attributable to the 1971 Spring Program merchandise in that warehouse as of December 31, 1970. (ADM HS 156-157, 178-182, 192-195; Botte Dep., pp. 178-183; Cook Dep., pp. 59, 62, 66-67, 74, 85, 95, 156-157, 159, 174-175, 278-279, 378-379)

Extended Dating

D75. In January 1970, Citibank became aware that Topper had given extended dating privileges on merchandise shipped in November and December 1969. Invoices on such merchandise were not payable according to their terms until May 10, 1970. (PX 667; Lusk Tr., pp. 1037-1038) In accordance with its normal policy to advance on receivables dated less than six months, Citibank treated the 1969-1970 extended dating receivables as eligible for advances. (PX 667; Lusk Tr., p. 1038)

D76. In December 1970, Citibank became aware that Topper was going to give extended dating on December invoices until May and August, 1971. (PX 680) As in 1970, the May dating was held eligible for advances by Citibank since it was due within six months. At first, Citibank determined that the August dating would become eligible when the May dating was paid (PX 680), but in February 1971 Citibank made the August dating eligible since such dating was then due within six months and eligible according to Citibank's normal policy. (PX 677A; Lusk Tr., p. 1043)

D77. During November and December, 1970, Topper made net sales of approximately $14 million on extended credit terms of 5 or 8 months pursuant to a 1971 Spring Program.

During the previous year Topper had made approximately $2 million of net sales on extended credit terms of 5 months. Topper's extended dating sales under its 1971 Spring Program accounted for approximately 22% of its 1970 net sales, compared with the prior year extended dating sales, which accounted for approximately 4% of Topper's 1969 sales. Prior to the Private Placement, these facts were known to Hayden Stone (HS ADM PF 229, 242-243; Weill Dep., pp. 89-90; Sterrett Dep., pp. 154-156; Sterrett AMEX Dep., pp. 88-90; PX 578), White & Case (ADM HS 39-41, 43-55, 69, 72, 78, 112; Hinsey Dep., pp. 57, 98, 103-106, 138-143, 267-270), Ford Motor Credit (HSX Ford 4, Schedule II, p. 2, Schedule III, p. 1; ADM HS 264), and all of the plaintiffs except for Local 816 Fund. (PX 462, Exhibit 1 at 6 (net sales 1969, 1970), 8, 34, (Note 3); PX 1401 at 1, ¶¶ 2-3; ADM 98)

D 78. During its 1970 audit of Topper Arthur Young knew that during November and December 1970 Topper made approximately $16 million of sales on extended credit terms of 5 or 8 months pursuant to a 1971 Spring Program, as compared with approximately $2 million of sales made on extended credit terms of 5 months the year before. (ADM HS 175) Arthur Young knew that after allowing for reserves of approximately $2 million, the 1971 Spring Program accounted for approximately 22% of Topper's 1970 net sales and that the extended dating sales of the previous year had accounted for approximately 4% of Topper's net sales for 1969. (ADM HS 185) Arthur Young knew that during the last four days of 1970 Topper shipped approximately $6.3 million, or 10%, of its 1970 net sales, with approximately $4 million, or 6% shipped on December 31, 1970, and that these sales represented merchandise aboard ships leaving the Orient on those days. (ADM HS 186) Arthur Young knew that in order to induce purchases under the 1971 Spring Program, Topper offered customers who ordered prior to December 31, 1970 an additional discount of 10%. (ADM HS 187; Botte Dep., p. 117)

D 79. Arthur Young knew that the 1971 Spring Program involved a promotion whereby Topper offered to store goods in the New York Terminal Warehouse on behalf of its customers, and that the terms of this warehouse program were embodied in an agreement between Topper and its customers called the Spring Promotion Warehouse Agreement and a letter from its customers to the New York Terminal Warehouse, known as a Warehouse Agreement. (ADM HS 158-159) Arthur Young examined both types of documents and knew that pursuant thereto all warehousing costs were to be assumed by Topper through September 1, 1971 and that the customers were required to remove all merchandise from the New York Terminal Warehouse by that date. (ADM HS 160-161)

D 80. During its 1970 audit of Topper Arthur Young took extended auditing steps to audit Topper's 1971 Spring Program because of the material amount and unusual nature of the warehousing and container shipment aspects of the Program. Included in these extended auditing steps was the sending of requests for confirmation of receivables to all customers who purchased merchandise pursuant to the 1971 Spring Program, requesting confirmation not only of the total balance owed Topper by the customer, but also separately of the balance attributable to the 1971 Spring Program, for which latter request copies of the 1971 Spring Program invoices were attached to the confirmation request. (Cook Dep., pp. 32 361-363, 367-371; Botte Dep., pp. 115-118, 128-130; ADM HS 156, 178-180; PX 961, 1050, 1059)

D 81. Included in the extended auditing steps undertaken by Arthur Young in its 1970 audit of Topper, were a review of the amount of merchandise returned by Kresge under a comparable program in 1969, a review of the merchandise stored in the New York Terminal Warehouse by customer and toy item, a review of confirmations and cash received from customers who had merchandise stored in the New York Terminal Warehouse, an examination of the Spring Promotion Warehouse Agreements, an inspection of the letters between the New York Terminal Warehouse and customers granting Topper the right to remove merchandise from the New York Terminal Warehouse, a review of customer order forms for merchandise stored in the New York Terminal Warehouse, a comparison of invoices to customer orders for merchandise stored in the New York Terminal Warehouse, and a review of the resolution adopted by the Topper Board of Directors authorizing the storage of merchandise in the New York Terminal Warehouse. (Cook Dep., pp. 364-367; ADM HS 157, 181-182)

D 82. With regard to merchandise shipped from the Orient under the 1971 Spring Program, Arthur Young obtained and examined a legal opinion from White & Case respecting passage of title to such merchandise, reviewed a confirmation request to the customs broker regarding merchandise shipped directly from the Orient, and tested bills of lading and other shipping documents relating to such merchandise. (Cook Dep., p. 364; Botte Dep., pp. 26-27; HSX Walsh Q; ADM HS 181, 201) In addition, Arthur Young employed the following auditing procedures with respect to such merchandise: inspecting invoices; inspecting receivable confirmations from customers; verifying goods shipped and testing them to orders and other documents; making confirmation requests to the customs broker; examining documents at the customs broker and verifying costs accrued in connection with the sales. (ADM HS 201; HSX Walsh Q)

D 83. During the 1970 audit, Arthur Young caused confirmation of receivables requests to be sent to all customers having a receivable balance with Topper as of December 31, 1970 of $1000 or more, whether or not such customers purchased merchandise pursuant to the 1971 Spring Program. (ADM HS 210) As of February 18, 1971, cash received by Topper in payment of December 31, 1970 receivables plus clean or cleared confirmations received by Arthur Young covered approximately 70% of Topper's December 31, 1970 receivable balance. The percentage for the 1971 Spring Program receivable balance covered by such confirmations was 71%. (ADM HS 214; Cook Dep., pp. 214-215; PX 1044) Kresge, which had purchased approximately $1 million in the 1971 Spring Program was among the customers who confirmed their 1971 Spring Program receivable balance. (ADM HS 213; PX 1057)

D 84. During the 1970 audit, Arthur Young received a confirmation response from the American Toy Company which stated that the $128,433.84 of extended dating invoices were not included in its records as of December 31, 1970. Following receipt of the response, Zoll of Arthur Young spoke with Rose of Topper who stated that American Toy was an obstinate customer which took discounts not allowed and then wouldn't pay the discount when requested. Arthur Young did further testing and learned that American Toy had received delivery of the extended dating merchandise sometime earlier in 1971. (ADM HS 212)

D 85. During Arthur Young's review of Topper's March 31, 1971 financial statements, Arthur Young updated its review of cash receipts and confirmations applicable to Topper's December 31, 1970 receivable balances. The result was cash receipts or clean or clear confirmations covering approximately 75% of that balance. (ADM HS 234; PX 1059)

D 86. As a result of numerous auditing steps including confirmation requests, Arthur Young concluded that Topper's 1971 Spring Program sales were properly reported as 1970 sales. (ADM HS 165, 191; Cook Dep., pp. 395-396)

D 87. Arthur Young required Topper to disclose the 1971 Spring Program in a separate footnote (Note 3) to its 1970 financial statements. Arthur Young drafted Note 3, which stated as follows:

> "NOTE 3 -- ACCOUNTS RECEIVABLE:
>
> Approximately $14,000,000 of sales made in December 1970 carried extended credit terms of five to eight months. The comparable amount for the prior year was $2,000,000."

(Cook Dep., pp. 385-387; ADM HS 197)

Miscellaneous Concessions

D 88. In some instances, a Topper representative granted a credit to a customer of Topper which was not reflected on Topper's books. (Samuels Dep., pp. 27-28; Cook Dep., pp. 235-238) This type of transaction included trans-shipments from one Topper customer to another, with no credit being given the former on the books of Topper. (Samuels Dep., pp. 30-31) Topper had an exchange program with some of its customers whereby customers returned certain merchandise with the privilege to obtain similar merchandise. In some case, such customers returned merchandise but credits for such returns were never recorded by Topper. (Samuels Dep., p. 39; Cook Dep., p. 237) In other cases Topper's customers obtained authorization for a return and returned merchandise, but were not issued an appropriate credit. (Samuels Dep., p. 40)

D 89. Similarly, some Topper customers were granted a credit to reimburse them for advertising Topper products (Samuels Dep., p. 41), or were issued mark-downs by Topper to assist the customer in selling merchandise, but such credits were never recorded on the books of Topper. (Samuels Dep., p. 42)

D 90. It has not been established that any person outside Topper, including Arthur Young, Hayden Stone, White & Case and Citibank, was aware that Topper had granted any concessions to customers without issuing appropriate credits and return authorizations.

D 91. Citibank was aware that Topper from time to time accepted from certain of its customers return of merchandise and exchanges of one type of merchandise for another for a number of reasons, such as when goods were damaged, delivered late or because of incorrect shipments of merchandise. (Lusk Tr., pp. 1059-1060; Siegel Tr., p. 1133) Citibank took such returns or exchanges into consideration in its calculation of the "dilution" of the Topper account, i.e., the difference between gross sales and net sales after all returns, discounts, allowances, rebates and other credits are taken into consideration. (Lusk Tr., p. 1055)

D 92. Citibank established reserves on its books against returns of Topper merchandise on a seasonal basis at the end of the year. These reserves, which amounted to no more than $2.5 million in any one year, were in addition to the 20 percent general reserve available under the 80 percent advance rate. (CBX 96; PX 675; Lusk Tr. pp., 1055-1059)

D 93. Topper reported to Citibank on practically a daily basis each of the various credits which any of its customers had notified Topper at that time it was taking. (PX 90-254) While each of the credit memoranda contained the same legend referring to "merchandise returns," the credits reflected therein were made for a number of reasons. Reasons for credits included rebates for the purchase of quantity merchandise, advertising allowances, various discounts, returns for damaged merchandise and returns in general. The credit memoranda do not indicate the individual reason why each credit was taken. (Siegel Tr., pp. 1197-1198) Some of the credits reflected in the credit memoranda were for 1970 merchandise, which were not issued by Topper until 1971 because the customers did not take a deduction for the credit until 1971. (Siegel Tr., pp. 1197-1198)

D 94. The total credits reflected on credit memoranda for January-August 1971 amounted to $5,669,929.15. (PX 1498)

D 95. Topper reported its returns in its monthly unaudited financial statements. Returns reported in Topper's June 30, 1970 financial statements for the first six months of 1971 were $500,000. (PX 2 at 25) In its September 30, 1971 financial statements, returns for the year to date were reported to be $1,177,000. (PX 5 at 27) Citibank's audit records showed that Topper's actual returns for the months July-October 1971 averaged about $343,000. (PX 703 at 3)

D 96. The amount of returns in the Topper account were typically modest, never substantial, and were never a matter of concern to Citibank. (Lusk Tr., pp. 1055-1059; Siegel Tr., pp. 1133-1134; Waldman Tr., p. 1215)

D 97. Prior to the Private Placement, Hayden Stone (HS ADM PF 231-233, 235), White & Case (ADM HS 113; Hinsey Dep., pp. 162-163), and Ford Motor Credit (ADM HS 280-282, 294-295; HSX Ford 4, Schedule II, p. 4, Schedule III, p.2), knew that in order to maintain customers' good will, Topper from time to time issued credits to certain customers for, among other things, rebates, mark-down allowance, price adjustments and advertising allowances.

D 98. Prior to the Private Placement, Hayden Stone (Byrnes AMEX Dep., pp. 115-117; Inglis AMEX Dep., pp. 40-42; Berlind AMEX Dep., pp. 257-258; Biondi SEC Dep., pp. 132-133), Arthur Young (ADM HS 135-136, 141-142, 144-145; Cook Dep., pp. 373-375, 391-394; Botte Dep., pp. 34-36; PX 958), White & Case (Hinsey Dep., pp. 162-163;, the Pension Fund (Thompson Dep., pp. 120, 387-388), and Connecticut Mutual (Hieronymus Dep., p. 35), as well as Citibank (Lusk Tr., pp. 1056-1058; Siegel Tr., p. 1133; Waldman Tr., p. 1215), knew that Topper had on occasion permitted customers to exchange non-defective unsold merchandise in order to maintain the customer's good will.

D 99. During its 1970 audit of Topper Arthur Young knew that in order to maintain customers' good will Topper from time to time permitted certain customers to return non-defective unsold merchandise for credit and issued credits to certain customers for, among other things, rebates, markdown allowances, price adjustments, and advertising allowances. (ADM HS 207-209)

D100. Arthur Young knew that at the end of 1969 and 1970 Topper accrued or reserved for the amount of credits it estimated would be granted customers for returns, discounts, rebates and allowances above and beyond the amount of credits already granted and recorded on its financial books and records. (ADM HS 215)

D 101. Arthur Young knew that the reserve for returns established against Topper's accounts receivable on both its December 31, 1969 and December 31, 1970 financial statements was $1 million, and that Topper had also established reserves on its December 31, 1970 financial statements for uncollectible accounts, for discounts and allowances, for rebates and advertising and for 1971 Spring Program sales stored in the New York Terminal Warehouse. Arthur Young audited the adequacy of each such reserve prior to certifying the December 31, 1970 financial statements. (ADM HS 218-221; PX 957-958)

D 102. Arthur Young knew that actual returns between March 17, 1969 and March 16, 1970 had been $1,596,978, and that actual returns between March 21, 1969 and March 20, 1970 had been $1,781,847. (ADM HS 222) Arthur Young also knew during the 1970 audit that the percentage of the difference between Topper's gross sales and net sales to its gross sales for its fiscal year ending in 1965 through 1970 had varied between 14.1% and 22.7%. (ADM HS 217; PX 1015)

D103. In the course of its Spring 1971 cold comfort review of Topper for its April 29, 1971 prospectus, Arthur Young learned that Topper had accepted or agreed to accept approximately $2 million in merchandise returns or exchanges during the first quarter of 1971. (ADM HS 233)

D104. Prior to the Private Placement, Ford Motor Credit knew that Topper's accounts receivable were subject to "frequent returns" and that Topper had established a reserve on its books of $2.5 million for returns expected during 1971. (HSX Ford 4, Schedule III, pp. 2-3; Pompea Dep., p. 73)

D105. The practice by Topper of occasionally permitting a customer to exchange merchandise which it could not sell for other merchandise was known as "balancing of inventory". (Rose Dep., pp. 156-158, 347-348; Byrnes AMEX Dep., pp. 116-117; Inglis AMEX Dep., p. 41; HS ADM PF 237; Cook Dep., p. 391; Thompson Dep., p. 388) During its 1970 audit of Topper Arthur Young determined that it was not necessary to make any reserve or other provision in Topper's 1970 financial statements with respect to Topper's balancing of inventory because its testing showed that the amount involved in balancing was "immaterial". (Cook Dep., pp. 392-393; Inglis Dep., p. 41; Byrnes AMEX Dep., pp. 116-117)

D 106. In early 1970 Topper developed a Johnny Lightning Exchange Program pursuant to which customers were permitted to return packages of unsold old models of Johnny Lightning cars to be repackaged with a mixture of newer model cars and reshipped to the customer. Arthur Young and Hayden Stone knew of this exchange program and considered it merely a form of inventory balancing rather than a right of exchange or return. (Cook Dep., pp. 21-22, 394-395; HS ADM PF 237; Sterrett Dep., pp. 40-42, 137-138; Sterrett AMEX Dep., p. 70)

D 107. Topper's monthly unaudited financial statements contained a schedule which reflected gross and net sales for the month entitled "Analysis of Shipments - Net." Among those on Topper's distribution lists for its June 30 and July 31, 1971 unaudited financial statements (PX 445, PX 452) were Topper's directors, including Roger S. Berlind and Sanford I. Weill of Hayden Stone and Joseph Hinsey of White & Case, Al Botte of Arthur Young, Ralph Pompea of Ford Motor Credit and certain individuals representing Citibank and Manufacturers Hanover. (PX 445, 452; Hinsey Dep., pp. 51, 58; ADM HS 305; PX 1262) In addition, the Pension Fund and Connecticut Mutual received Topper's June 30, 1971 unaudited financial statements as part of the Examples of Company's Reporting (PX 1459). Thompson noted therein that "the gross sales figure was about 21 million and the net sales figure was about 19 million." (Thompson Tr., p. 527)

Outsiders' Lack of Knowledge of Rights of Return or Exchange

D 108. To induce purchases pursuant to the 1971 Spring Program, Topper in November and December 1970 agreed with certain customers to grant a right of exchange applicable to said purchases. With certain of these customers Topper further agreed to embody this right in a letter. Exchange letters were written to at least 21 customers who ordered pursuant to the 1971 Spring Program. Topper also issued exchange letters to certain customers in 1971 to induce such customers to accept Topper merchandise during this period. (HS ADM PF 146, 148, 150) Such letters issued in connection with the 1971 Spring Program typically contained language such as the following:

> "This memo is to confirm that we will exchange any excess merchandise from your 1971 Spring Order on a dollar for dollar basis for any merchandise in our 1971 line."

(PX 833, 838, 840, 844, 849, 873-874, 876, 878, 881, 883-888, 890-893, 895-896, 1100, 1333, 1343, 1346)

D109. Orenstein and Pierce kept secret from outsiders and other employees the existence of Topper's written and oral agreements or arrangements with many of its customers pursuant to which customers were given rights to return or exchange non-defective excess merchandise or to pay for such merchandise only when resold by the customer. (Pierce Dep., pp. 210-213; Hinsey Dep., p. 299; Rose Dep., pp. 336, 353-364; AYX 1-2; Obolsky Dep., pp. 113-115, 125-129, 147-149; Sterrett Dep., pp. 155-158; Ramseur Dep., pp. 220-221; PX 837) Pierce maintained a confidential personal file in which all such written agreements were kept, at the instruction of Orenstein. (Pierce Dep., pp. 211-212; AYX 1, p. 4)

D 110. During Arthur Young's 1970 audit of Topper, in connection with its sending of requests to Topper's customers for confirmation of accounts receivable, certain Topper customers were told by Orenstein or Pierce or another employee in Topper's sales department that they should answer such confirmation requests without mentioning their rights to return or exchange non-defective excess merchandise or to pay for such merchandise only when resold by them. Calls were made to such customers for that purpose as a result of Topper's hearing from many of its customers that they were concerned that if they answered their confirmation requests positively, "they might in some way jeopardize the right they had to exchange merchandise dollar for dollar pursuant to their agreements with Topper". (Pierce Dep., pp. 211-214, 371-382; Hughes SEC Dep., pp. 108-113; AYX 3, 3A, 3B; Sieff Dep., pp. 83-90; HSX Sieff 1) In the course of such calls, the customers were told that they need not be concerned that they would lose their rights of exchange because a confirmation request was not a legal document and did not detract from their contractual agreements with Topper. (Pierce Dep., 213-217; AYX 3, p. 2)

D 111. No Citibank representative was, prior to December 1971, aware that Topper was extending any rights to return or rights to exchange or rights to redate any merchandise, or that Topper or any of its customers felt that Topper's customers had a right to return or exchange any significant amount of merchandise. (Lusk Tr., p. 1059; Siegel Tr., p. 1134; Waldman Tr., pp. 1216-1217)

D 112. Prior to the Private Placement Hayden Stone did not know of the existence of any agreements or arrangements, written or oral, between Topper and any of its customers pursuant to which a customer was given a right to return or exchange non-defective excess merchandise or to pay for such merchandise only when resold. (Weill Dep., pp. 144-151; PX 564; Sterrett Dep., pp. 39-45, 132-133; Byrnes AMEX Dep., pp. 116, 179-180; Inglis AMEX Dep., pp. 40-42; Berlind AMEX Dep., pp. 196-197; Sterrett AMEX Dep., pp. 67-71, 139-140; Biondi SEC Dep., pp. 132-133)

D 113. Prior to the Private Placement Arthur Young did not know of the existence of any agreements, written or oral, between Topper and any of its customers pursuant to which a customer was given a right to return or exchange non-defective excess merchandise or pay for such merchandise only when resold. (ADM HS 138-139, 190, 241; Zoll Dep., pp. 152-153; Botte Dep., pp. 34-38; Cook Dep., pp. 65-66, 277-285, 335-337, 371-391, 406-411, 426-429; PX 1091-1092 (Tr., pp. 750-751); PX 1101 (Tr., p. 69); PX 1117 (Tr., p. 73); CBX 121; HSX Zoll 1)

D 114. Prior to the Private Placement White & Case did not know of the existence of any agreements, written or oral, between Topper and any of its customers pursuant to which a customer was given a right to return or exchange non-defective excess merchandise or pay for such merchandise only when resold. (ADM HS 119; Hinsey Dep., pp. 59, 100-101, 296-297; Provine Dep., pp. 40-41; ADM HS 79, 111)

Citibank's Decisions as to Topper Business Practices

D 115. All of Citibank's decisions with respect to Topper's extended dating receivables, redated receivables, warehoused merchandise and returns and exchanges were made in accordance with normal and prudent commercial financing practice. (Silverman Tr., pp. 1285-1286)

V. Pension Fund Investigation

Background

D 116. Thompson obtained a Masters of Business Administration from Harvard Business School in 1959. Thompson became a chartered financial analyst in approximately 1966. Upon graduation from the Harvard Business School, Thompson worked for an institutional brokerage firm for approximately seven years from 1959-1966 as a securities analyst, doing securities analysis for institutional clients including banks, insurance companies and pension funds. (Thompson Tr., pp. 374-375)

D 117. From 1966 to 1969, Thompson was an assistant portfolio manager with the Federal Insurance Company, making recommendations on stock and bond securities. (Thompson Tr., p. 376)

D 118. In 1969 Thompson joined the Pension Fund as its investment manager, responsible for public and private financings and sale and leasebacks in the drug, retail trade, non-ferrous metals, cosmetics and textile industries as well as companies specifically assigned to him by Molé, the President of the Pension Fund, to whom Thompson directly reported. (Thompson Tr., pp. 377-379)

D 119. In 1971 the Pension Fund, which had assets of over $3 billion (Thompson Tr., p. 496), employed ten persons in the area of investment analysis including, in addition to Thompson, Molé as President, Harrison and Van Deusen as vice-presidents, and six security analysts. (Thompson Tr., pp. 379-380)

D 120. Prior to the Summer of 1971, Thompson had read various research studies on the toy industry; had participated in meetings with the managements of Mattel and Ideal and had bought Milton Bradley stock. (Thompson Dep., pp. 37-40, 52-56)

D 121. In the Spring of 1970, Thompson received a preliminary prospectus on Topper's 1970 public offering from Hayden Stone. He later received a phone call from Nick Luongo, the Hayden Stone salesman who serviced the Pension Fund account. (Thompson Tr., pp. 498-499) Luongo recommended an investment in the public offering. Thompson told Luongo he had read the prospectus and that the Pension Fund had no interest at all in investing in Topper because of Topper's "turbulent past history" and its highly leveraged capitalization. (Thompson Tr., pp. 499-500; Thompson Dep., pp. 79-80; ADM 107)

D122. Shortly thereafter, Luongo invited Thompson to lunch and again recommended Topper as an investment. Thompson again declined, citing the same reasons. Thompson cut Luongo off and, in effect, told Luongo not to waste his time and that Topper was not a prudent investment for a pension fund. (Thompson Tr., p. 500; Thompson Dep., pp. 80-81; ADM 107)

D123. After Thompson's lunch with Luongo, Glover Johnson, a partner of White and Case whom Thompson knew was a director of Topper, called Thompson to recommend an investment in the Topper 1970 public offering. Thompson told Johnson he was not interested. (Thompson Tr., p. 499; Thompson Dep., pp. 81-82; ADM 70-71)

Private Placement Memorandum and Prospectus

D 124. Thompson was first contacted concerning the Private Placement by Inglis of Hayden Stone, who called Thompson in late July, 1971. (Thompson Tr., pp. 389-390)

D 125. Inglis said Hayden Stone was Topper's investment banker and recommended an investment in the Private Placement. Thompson told Inglis he had looked at Topper once before and had not considered it an appropriate investment because of its past history and the large amount of its borrowings relative to equity. Inglis said Topper was a much different company in 1971 than in 1970, as it had more stability and was less dependent upon seasonal factors. (Thompson Tr., pp. 500-501; Thompson Dep., pp. 86-87)

D 126. Inglis tried to arrange a meeting between the Pension Fund and Topper management. Thompson declined Inglis' invitation to meet with Topper management at that time and asked Inglis if Hayden Stone had prepared anything in writing about Topper. In response, Inglis sent Thompson a copy of PX 462, the Private Placement Memorandum, together with its exhibits, including the April 1971 Prospectus, which Thompson felt was an integral part of the Private Placement Memorandum. (Thompson Dep., pp. 86-87; ADM 109)

D 127. The Introductory Statement of the April 1971 Prospectus included the following statements:

> "This offering is speculative in nature and the prospective investor should be aware of the following information:
>
> 1. The Company suffered a net loss of $18,715,000 for the period from October 4, 1966 to February 4, 1967 and a net loss of $833,000 for the period from February 5, 1967 to December 31, 1967, and its business predecessor suffered a net loss of $8,622,000 during the first nine months of 1966. . . .
>
> 2. A significant portion of the toys manufactured by the Company are marketed for no longer than a few years and, consequently, the Company's business is largely dependent upon its ability continually to develop new products. . . .
>
> 3. The Company imports, primarily from Japan and Hong Kong, substantial amounts of products and components. The Company is thus subject to the risks inherent in depending upon foreign suppliers, including the potential for delays in deliveries, losses and damages in transit and the imposition of import and export duties. . . .
>
> 4. The Company's operations are dependent in large part upon the continuation of its bank borrowings, which are payable on demand. . . .
>
> * * * *
>
> 6. Mr. Henry Orenstein, President of the Company, has an instrumental role in day-to-day operations -- particularly with regard to product development and the creation of advertising -- and his unavailability for any reason would have an adverse effect upon the Company and its business. . . .

> 7. There can be no assurance that the Company will not require additional financing of a long-term nature, and, if such financing is required, that it will be available on reasonable terms." (PX 462, Exhibit 1 at 3-4)

D 128. Included as Note 3 to the financial statements in the April 1971 Prospectus was the following statement:

> "Approximately $14,000,000 of sales made in December 1970 carried extended credit terms of five to eight months. The comparable amount for the prior year was $2,000,000." (PX 462, Exhibit 1 at 3-4)

D 129. In addition, the April 1971 Prospectus stated as follows:

> "The Company is engaged in a very competitive business and has been required to meet extended dating offered to customers by competitors, thus increasing the Company's needs for and costs of working capital. December 1970 sales included approximately $14,000,000 of shipments, which consisted primarily of spring program merchandise, carrying extended terms of five to eight months, compared to similar sales of approximately $2,000,000 in 1969." (PX 462, Exhibit 1 at 8)

D 130. The April 1971 Prospectus showed total 1969 net sales of $53,722,774 and total 1970 net sales of $63,935,619. (PX 462, Exhibit 1 at 6)

D 131. The April 1971 Prospectus stated that one reason

> "for the substantial decline in sales and the very large losses incurred during the thirteen months ended February 4, 1967 [was] the liquidation of large quantities of inventories at substantially reduced and close-out prices." (PX 462, Exhibit 1 at 8)

D 132. The April 1971 Prospectus stated another reason for such losses as follows:

> "As a result, in part, of the disruption of normal marketing created by such large inventory liquidations, customers returned approximately $4,200,000 of toys sold to them under "bill and hold" arrangements in 1965 and allowances were made to customers of $900,000 against sales made in 1965." (PX 462, Exhibit 1 at 8)

D 133. The April 1971 Prospectus also stated as follows:

> "The business originally involved the marketing of toys through supermarkets pursuant to a program, introduced by Henry and Marrius Orenstein in 1953, which permitted retail outlets to return unsold merchandise ordered for sale during the Christmas season. DeLuxe Reading Corporation acquired the business from the Orensteins in 1960 and, in 1964, began eliminating its supermarket business; at the same time it began marketing its products through conventional toy outlets. In October, 1966, toward the end of this period of transition from supermarket to conventional outlets, Henry Orenstein ... joined Marrius Orenstein and a group of ten other investors ... to repurchase the business ...." (PX 462, Exhibit 1 at 9-10)

D 134. The Private Placement Memorandum stated as follows:

> "The excellent reception to the Spring program and first quarter results indicate that Dawn, as well as the Company's other low-priced products, appears to be selling on a year-round basis and should serve to reduce the Company's seasonal volume and earnings fluctuations." (PX 462 at 6)

D 135. When Thompson first read the Private Placement Memorandum, three things stood out in his mind: (1) Topper had gone into a program of selling Dawn dolls,which had been introduced in early 1970 and which Topper said would cut down on the seasonal fluctuations in its business and provide stability to Topper; (2) Topper felt that Sesame Street, with which it had become associated in March 1971, would be a staple item in the educational section of the toy market that would broaden Topper's market base and had good growth prospects and (3) the projections in the exhibits to the Private Placement Memorandum presented Topper at the end of 1971 as being in good financial condition, making about $5 million in pre-tax profit, with cash inflow exceeding cash outflow by more than $27 million and short-term borrowings repaid, or with about $5 million of cash to invest in government securities or whatever Topper chose. (Thompson Tr., pp. 390-391)

D 136. Thompson knew from the Private Placement Memorandum that Topper had gone into a Spring 1971 Program, mentioned "prominently" in the April 1971 Prospectus (Thompson Dep., p. 103), whereby Topper had shipped in December 1970 $14 million of merchandise which would be paid for in 1971, that $11 million of this merchandise was Dawn merchandise, and that Topper's total 1970 sales had been $64 million. (Thompson Dep., p. 96; ADM 98)

D 137. Principal risk factors of the April 1971 Prospectus to Thompson were that Topper through 1968 had a history of substantial losses, that it was dependent upon bank financing, and that it appeared to be a one-man company. (Thompson Tr., pp. 506-507)

D 138. From the Topper income statements in the Private Placement Memorandum, Thompson concluded that Topper had in the past suffered substantial losses, but that if discontinued operations were excluded, Topper was increasing its profitability. (Thompson Tr., pp. 390-393)*

D 139. There was no doubt in Thompson's mind throughout his investigation that the proceeds from the Private Placement were to go to the Lending Banks. (Thompson Tr., pp. 495-496)

D 140. Thompson read the financial statements and knew they were certified by Arthur Young, Topper's auditors, but was not aware that Arthur Young had given Topper a cold comfort letter in 1971 nor that issuers were required in connection with a public offering to obtain an update of their most recent certified financial statements from their accountants. (Thompson Tr., pp. 507-508) Certification of financial statements by independent auditors was a prerequisite to investment by the Pension Fund. (ADM 100)

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*In his deposition, Thompson said that he came to no conclusions on the basis of reading the Private Placement Memorandum, and that nothing therein changed his thinking from the way he thought in 1970. (Thompson Dep., pp. 93-94)

D 141. Thompson understood that Topper did not expect to have any short-term bank borrowings by the end of 1971 and thereafter. (Thompson Tr., pp. 511-512; ADM 106)

Thompson Visit to Topper

142. Thompson agreed to meet with Topper management and Inglis arranged a meeting on August 4, 1971. Thompson met first on August 4 with Inglis at Inglis' office. Thompson explained why he had declined to invest in Topper and asked why Inglis felt Topper had more stability than when Thompson had looked at it before. Inglis said that Topper had gone into a program of Dawn dolls, which was a low-priced item which would sell year-round, and that this program was giving Topper stability. Inglis also said that Topper had obtained common stock financing in April 1971. (Thompson Dep., pp. 90-91)

D 143. Thompson spent a good deal of time in his meeting with Inglis discussing whether the Dawn merchandise was moving and had been sold, and what controls Topper had to make sure in fact that the merchandise was sold. Inglis told Thompson that Orenstein monitored the sale of goods over the counter and that Hayden Stone in connection with the 1971 public offering had made inquiry to be sure that Dawn goods which were shipped were actually sold by Topper's customers and that the Spring Program was a success. He also said that Hayden Stone had compared the terms of Topper's 1971 Spring Program with those of a comparable Mattel program and had found out that Topper's terms were shorter and its customers had less time to pay than the Mattel customers. Inglis told Thompson that Hayden Stone had assured itself that the Dawn merchandise was moving well at the retail level, that this had been a very successful program that would lend stability to Topper and that Topper was actually reordering more Dawn dolls and looked forward to a similar program in 1972. (Thompson Dep., pp. 100-105)

D 144. Thompson inquired as to what financial controls Topper had. Inglis said that Topper had a very elaborate computer system for checks on whether shipments were being made relative to orders and as to accounts receivable and inventory. (Thompson Dep., p. 106)

D 145. Inglis and Thompson also discussed the Topper-Hayden Stone relationship. Inglis said there had been a long relationship between Hayden Stone and Topper, encompassing several financings including the 1970 and 1971 public financings, since the purchase of Topper from Philadelphia and Reading. Inglis said that Topper was the largest personal holding of Berlind and Weill and that they were on Topper's Board. Thompson felt that Hayden Stone had been very active in the April 1971 financing and was totally on top of the situation. (Thompson Dep., p. 108)

D 146. After their meeting, Thompson and Inglis went to Topper's New York showroom, where Inglis introduced Thompson to Orenstein. (Thompson Dep., p. 111) During a tour of the Topper product lines at the showroom, Thompson questioned Orenstein about the Dawn line. The Dawn product was obviously important to both Thompson and Orenstein. (Thompson Dep., p. 113)

D 147. Orenstein stated and Inglis confirmed that the Dawn line was doing well and that additional Dawn merchandise was being reordered to replace the Dawn products that had already gone into the hands of children. (Thompson Tr., pp. 393-394)

D 148. Orenstein showed Thompson Topper's Suzy Homemaker, Smarty Pants and Johnny Lightning products. During this tour

Orenstein mentioned that Mattel had loaded up the trade with its product Hot Wheels at the end of the previous selling season and the trade was angry with Mattel, and that this had and would help Topper in selling the Dawn line. (Thompson Dep., pp. 112-113)

D 149. Thompson's tour at the showroom ended with the Sesame Street merchandise. Orenstein told Thompson that this merchandise would be a stabilizing influence in Topper's business, and mentioned that Topper's arrangement with the Children's Television Workshop went on until December 31, 1974. (Thompson Dep., p. 114)

D 150. After the tour of the Topper showroom, Orenstein's chauffeur drove Thompson, Inglis and Orenstein to Topper's plant in Elizabeth, New Jersey. Upon arriving at the plant, Thompson went to Orenstein's office where he and Orenstein talked again about the Dawn line. (Thompson Dep., pp. 115-116)

D 151. Orenstein told Thompson he had talked that morning with Glover Johnson from White & Case and that Johnson was available to talk to Thompson about Topper, and encouraged Thompson to do so. (Thompson Dep., p. 116)

D 152. Thompson then talked with Rose, Topper's chief financial officer, about the types of controls that Topper had with respect to receivables and inventories. (Thompson Dep., p. 118)

D 153. During his discussion with Rose, Thompson brought up the subject of consignment sales because there was a reference in the Topper Prospectus to a past period when the company had returns of over $4 million due to a bill and hold program, and also a reference to sales to supermarkets which had been returned and resulted in substantial losses. This subject was discussed with Rose in the context of whether Topper's sales were final. (Thompson Tr., pp. 394-395)

D 154. Thompson and Rose discussed in detail, but did not look at, the documents which Rose said Topper had in order to prevent a recurrence of these past problems. Rose said that Topper had agings of receivables, cash flow projections and reports which indicated that Topper had enough of a lead part to produce a particular toy but was not overstocked on the standard parts that went into it. Rose also said that Topper worked very closely with Citibank and that Citibank was receiving the information relating to collections and agings of receivables. (Thompson Tr., pp. 395-396) Rose said he was in almost daily contact with Citibank (Thompson Dep., p. 119)

D 155. Thompson and Rose were just getting to the point where Thompson was going to look at these documents* when Rose said "Mr. Orenstein is going to have lunch with you in a few minutes.* Let us go down and actually see the documents produced at the other end of the hall in the computer room." Thompson and Rose then went to the computer room and saw the IBM machinery. Coming back down the hall, Thompson asked Rose ". . . are your sales final?" Rose answered "Yes, they are." Thompson asked ". . . what about returns?" Rose answered ". . . we are very hard-nosed about returns." (Thompson Tr., p. 396; Thompson Dep., pp. 120, 387)

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* The last page of each of Topper's monthly aging reports, which Thompson discussed with Rose but did not look at, contains a summary of the agings of all of Topper's receivables. The report for July 31, 1971, for instance, shows over $8 million receivables in the "90-day" column. (PX 352)

D 156. With regard to Topper's accepting returns from its customers, Thompson asked, "Don't you ever do it basically?" Rose responded, "Well, sometimes we will balance one good selling toy with another." Thompson then asked, "Well, what about one that is not selling well?" Rose responded, "Well, we definitely don't take back the ones that are not selling and we discourage this." (Thompson Tr., pp. 397-398)

D 157. Thompson did not ask to see any contract between Topper and any of its distributors nor did Rose show him any. (Thompson Tr., p. 397)

D 158. Thompson then asked Rose what Topper's bad debts were likely to be from the accounts they were dealing with, and Rose indicated they would be under $200,000, and probably about $150,000. (Thompson Tr., p. 398)

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*Thompson did not respond to the Court's question as to what documents he was going to see when Rose suggested he have lunch instead. (Thompson Tr., pp. 396-397)

D 159. During lunch on August 4, Orenstein assured Thompson that the toy business had more stability than in the past and that the Dawn program was a successful program. (Thompson Tr., p. 398)

D 160. After lunch, Orenstein took Thompson on a complete tour of the Topper facilities. Thompson talked with a Topper employee whose job was to estimate the cost of new toys, and the employee in charge of new product development. He then reviewed the Sesame Street toy lines and a line of action toys, including the Dawn accessories. Thompson asked whether there were any other controls in addition to the computer arrangement to check that goods are actually moving. He was shown a box of snapshots of Dawn displays in stores which snapshots had been taken by Topper's salesmen. Inglis added that these snapshots confirmed what Hayden Stone knew - that Dawn was a success. (Thompson Dep., pp. 123-125)

D 161. Rose and Thompson then went from the Topper office building to the plant facilities. On the way, Thompson raised with Rose the subject of Remco's problems, of which Thompson was generally aware. Rose said that Remco's problem was due to a lack of control over inventory.(Thompson Dep., p. 126)

D 162. Thompson then toured the plant with Cassata and Rose. After his tour, Thompson was asked to view commercials at Dancer Fitzgerald, Topper's advertising agency, and left for New York with Orenstein, Inglis and Jack Jones, the new Topper officer in charge of promotion. (Thompson Dep., pp. 127-129)

D 163. On his trip back to New York from New Jersey, Thompson asked Orenstein about Topper's relationship with the Lending Banks. Thompson asked who at Citibank was responsible for the Topper account, and Orenstein said that Waldman was the senior man on the account. Thompson asked Orenstein if he was free to talk to Waldman and Orenstein said he was. Thompson also told Orenstein he was probably going to make trade checks of who on Wall Street followed the toy stocks. (Thompson Tr., p. 399)*

D 164. Returning to New York, Thompson, Orenstein and Jones went to the offices of Dancer Fitzgerald and viewed

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*Thompson testified at trial that the most important point about the trip back to New York was that Orenstein had given him the name of a person at Citibank to contact and that he had been given the green light to do so. (Thompson Tr., pp. 399-400) During his deposition, Thompson testified that a "quite important" point which came up during the trip was Thompson's saying that the Pension Fund usually did trade checks and his asking if this was all right. He felt that Orenstein tried to direct him to particular Topper customers who would give Topper a favorable report. (Thompson Dep., pp. 132-133)

Topper commercials. (Thompson Dep., pp. 133-134)

D 165. Upon returning home on the night of August 4, Thompson made notes of his trip (PX 1371) and on August 5, 1971 dictated PX 1372, a memorandum to Molé on his visit to Topper. Thompson delivered PX 1372 to Molé that day or the next. (Thompson Tr., pp. 400-401)

D 166. PX 1372 made no mention whatsoever of Citibank (PX 1372).

D 167. The last sentence of PX 1372 states as follows: "If you concur, I would like to do this deal." (PX 1372)

Thompson Discusses Topper with Molé

D 168. Mole at that time was going on vacation. Thompson and Mole discussed PX 1372, particularly the points that Dawn and Sesame Street seemed to be giving more stability and that Topper had a good set of financial controls. Mole told Thompson that the Pension Fund had some special relationships that Thompson could check out. Mole told Thompson that while Mole was away, Thompson should check with Glover Johnson. Mole also approved making trade checks and told Thompson to get Topper's 1970 annual report and any interim financials that had come out. (Thompson Tr., pp. 403-404)

D 169. Upon reading PX 1372, Mole felt that Topper was an unusual investment for the Pension Fund, but appeared to have less risk than first met the eye, because its toy business was 60 percent low price items so that there seemed to be less cyclicality and seasonality and because Topper had Sesame Street. At that time or soon thereafter, Thompson and Mole discussed the need for a registration statement as a means of getting out of an investment in Topper. (Mole Tr., pp. 659-661)

Further Inquiries by Thompson

D 170. During the week of August 9, Thompson asked Rose to come to his office to show Thompson Topper's financial control system and do more than just discuss it in general. (Thompson Tr., p. 405)

D 171. On August 10, Thompson read Dan Dorfman's Wall Street Journal column "Heard on the Street" about Topper. (PX Richards 1) The article implied that there was a much less exclusive relationship between Topper and Sesame Street than Thompson had been led to believe by Orenstein. (Thompson Tr., p. 514; Thompson Dep., pp. 139-140)

D 172. Dorfman described Topper's results as "erratic" and its balance sheet as "far from the strongest." The article said that William Schwartz, one toy industrial specialist, was advising his clients to avoid any new purchase of Topper stock, but that it could be held as a "speculation". (Thompson Tr., p. 515; PX Richards 1)

D 173. A second analyst was described in the article as saying that Topper's balance sheet did not excite him, and observed that about $14 million of 1970 sales came from customers given five to eight months to pay their bills. (Thompson Tr., pp. 517-518; PX Richards 1)

D 174. A third analyst was reported as stressing that the Topper stock was not "for widows and orphans." and that "a lot of things could go wrong," including the possibility that such Topper product lines as the Dawn dolls might not live up to sales projections. (Thompson Tr., p. 517; PX Richards 1)

D 175. Thompson saw the statement in the Dorfman article that Orenstein could not make any comment upon earnings because Topper was in registration, but did not ask anyone what registration Topper was in or review any prospectus relating to such registration. (Thompson Tr., pp. 518-519)

D 176. After Thompson had read the Dorfman article, Orenstein called him to tell him that Topper had a relationship whereby if Sesame Street accepted one of the Topper toys it became a Topper exclusive, or if Sesame Street asked Topper to develop a particular toy, Topper had all the rights to such toy. Orenstein said that Sesame Street was not considering replacing Topper and that this subject was greatly overblown.

Orenstein referred Thompson to Christopher Cerf at Childrens Television Workshop. (Thompson Dep., p. 142)

D 177. On August 10, Thompson called Cerf, who told him that the Sesame Street line of toys would have an expectancy of five or six years. Cerf confirmed the relationship with Topper whereby if Topper developed a specific toy which Sesame Street approved, Topper had an exclusive on the toy. Cerf said he was thrilled with the Topper-Sesame Street relationship and confirmed what Thompson had been told and read in the Private Placement Memorandum about Sesame Street adding a dimension of stability to Topper's business. (Thompson Tr., p. 406)

D 178. Also on August 10, Thompson called Bill Schwartz of Burnham & Company, a securities firm. Schwartz was one of the toy securities analysts who had been mentioned in the Dorfman article on Topper. (Thompson Tr., pp. 420-421, 513-514) Schwartz advised Thompson against an investment in Topper and said he had given the same advice to five other people who had contacted him. (Thompson Dep., p. 144) Thompson did not ask Schwartz who the others were who had been advised against Topper and Schwartz did not tell him. (Thompson Tr., p. 519; Thompson Dep., p. 144) Nor did Thompson ask Schwartz whether Topper sold goods on a final sale or consignment basis. (Thompson Tr., p. 519)

D 179. Schwartz said he advised against Topper because Topper's product life was shorter than Mattel's, Topper was a "high roller" in advertising expenditures, and because Orenstein had misled Schwartz regarding Topper's discontinuance of its Youth Care line of products. (Thompson Dep., pp. 144-145)

D 180. Thompson did not contact any of the other security analysts mentioned in the Dorfman article about Topper. (Thompson Dep., p. 147)

Trade Checks

D 181. Thompson called one member of the founding family of Zayre, an executive vice-president, and asked him if he would have the person most knowledgeable about Topper call him. (Thompson Dep., p. 138) The Pension Fund had done a private placement of Zayre, which was a department store chain and a customer of Topper. (Thompson Dep., p. 151) On about August 11, Thompson received a call from Hessdorf, the toy buyer for Zayre, and made a memorandum of the conversation. (PX 1375) Hessdorf said Orenstein was very important to the marketing side of Topper's business and that the marketing personnel beneath Orenstein were thin. Hessdorf said he had no knowledge of Rose or Jones. (Thompson Dep., p. 150) Hessdorf said that Topper deserved credit for its Dawn program and that it was successful, but that Mattel's Barbie Doll still dominated the doll industry even after 10 years in its price bracket. (PX 1375; Thompson Tr.,

p. 521) Hessdorf said that the trade was looking for a strong number two company to Mattel, citing the instance where Mattel had loaded the trade up with Hot Wheels. Hessdorf said that the trade was angry with Mattel because the trade had not really been willing to take this merchandise, that Mattel did not "make it up to them," and that the trade was "laying in wait" for Mattel and very willing to do business with Topper. (Thompson Tr., pp. 409-410)

D 182. Thompson asked Hessdorf if Topper's management was honest. Hessdorf said he felt they were. Thompson asked Hessdorf about Schwartz' criticism that Topper's product life was shorter than Mattel's. Hessdorf disagreed, saying that Topper could go longer into the selling season than anyone else in the trade. (Thompson Tr., p. 410)

D 183. Thompson did not discuss Topper's marketing methods with Hessdorf. (Thompson Dep., pp. 150-151)

D 184. Thompson concluded from his talk with Hessdorf that the Dawn program was successful and the trade was looking for a good number two company. He also concluded that Orenstein seemed to be dominating the marketing side of Topper. (Thompson Tr., p. 411)

D 185. Thompson did not ask Hessdorf about Topper's return policies or what was common in this regard in the toy industry, or whether his company had rights of return or exchange or what recourse he might have if he were overstocked. (Thompson Tr., pp. 411-412; Thompson Dep., pp. 494-495)

D 186. Thompson called the assistant treasurer at J.C. Penney, with whom Thompson had some months previously concluded a sale and lease-back transaction, and asked him if he would have the person most knowledgable about Topper call him. (Thompson Dep., p. 138) On or about August 11, Thompson received a call from Mr. Folan, the toy buyer at J.C. Penney, and made a memorandum of the conversation (PX 1376). Folan told Thompson that Topper management was honest and hardworking. In contrast to Hessdorf, Folan said Topper had a competent middle management.* Folan criticized Topper for spending a high percentage of revenue on television advertising. Folan said that the Dawn Program was a success and that the outlook for the Sesame Street line was good. (Thompson Tr., pp. 407-408; PX 1376)

D 187. Thompson did not discuss with Folan the marketing methods of Topper or the payment provisions of Topper sales. (Thompson Dep., pp. 155-156) Similarly, Thompson did not ask Folan anything about Topper's return policies or those of the toy industry, or whether his company had rights of return or exchange, or what recourse he might have if he were overstocked. (Thompson Tr., p. 408; Thompson Dep. pp. 494-495)

D 188. Thompson asked Folan whether he thought Topper was a suitable investment for the Pension Fund from a risk standpoint. Folan asked Thompson if he had read the April 1971

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*Folan did not mention any individuals and did not, in fact, know of Rose. (Thompson Dep., p. 166)

Prospectus. Thompson said he had and that this was in part why he asked Folan the question. Folan replied that his relationship with Topper was good and he had been doing an increasing amount of business with Topper. (Thompson Dep., pp. 167-168)

D 189. Thompson asked Folan if Topper was likely to be in business in another 10 years, and Folan paused before answering that he thought so. (PX 1376) Thompson did not ask Folan why he paused. (Thompson Tr., p. 522)

Further Discussions

D 190. On August 12, 1971 Thompson had a telephone conversation with Glover Johnson, a director of Topper and a partner in the law firm of White & Case, Topper's lawyers, as well as attorneys for United States Steel. PX 1371 is a copy of notes dictated by Thompson concerning that phone conversation. (Thompson Tr., pp. 412-413)

D 191. Thompson called Johnson to check on the integrity of Topper management from someone who was "like the people" at the Pension Fund, knew the Pension Fund well and was an honorable man, and to get some background on the past history of Topper and how a company which had suffered losses could be a suitable investment for a pension fund. (Thompson Tr., p. 413)

D 192. Thompson asked Johnson how he became involved with Topper. Johnson said he became involved in the purchase of Topper from Philadelphia & Reading, and that Topper had gotten into trouble in the past when they were shipping out merchandise in December and recording such shipments as sales and profits in December, resulting in a manipulation of Philadelphia & Reading's earnings. Johnson said that Henry Orenstein had wanted that consignment selling stopped, that the practice of selling on consignment had ended and that this was the principal reason for Orenstein's repurchase of Topper from Philadelphia & Reading. (Thompson Tr., pp. 414-415)

D193. Thompson asked Johnson about Orenstein's integrity. Johnson said Orenstein was honest and hard working and gave Thompson a brief description of Orenstein's background. (Thompson Tr., p. 415)

D194. Later on August 12 Thompson gave Harrison a copy of the Private Placement Memorandum in preparation for a meeting with Topper the next day. Harrison told Thompson that he had checked out Topper with a personal friend who was with Louis Marx, a toy manufacturer, and that he had visited a toy store and looked for Topper products. Harrison said that his friend considered the toy business on a comparable level with the garment business. (Thompson Dep., pp. 178-179; ADM 126) Harrison took this statement to mean that the toy industry was very competitive. (Harrison Dep., p. 9)

August 13 Meeting

D 195. In preparation for a meeting on August 13 with Rose and Downs, Thompson reread the Private Placement Memorandum and his memoranda concerning Topper. (Thompson Dep., p. 182)

D 196. On August 13, 1971 Thompson and Harrison had a meeting with Rose and Downs for about two and one half hours and over lunch. (Thompson Dep., p. 182) Downs described the growth in the toy industry and the fact that the larger companies such as Topper were getting an increasing share of the business. Downs said that Orenstein was monitoring the flow of goods at the retail level and that the Dawn program was successful and that Topper's customers had reordered merchandise. He discussed the Spring Program trade brochure on Dawn and said Topper was going to do a similar program at the end of 1971. (Thompson Tr., pp. 416-417)

D 197. Thompson and Downs discussed the importance of Henry Orenstein to Topper. Downs said that the trade viewed Topper as it had been a year or so earlier, when Orenstein had in fact dominated the marketing side, but that Topper now had Orenstein in more of a supervisory role, but still contacting important clients. Downs said Topper had brought in Jack Jones to be in charge of promotion and Fred Pierce in charge of sales. (Thompson Tr., p. 417)

D 198. The Sesame Street product line and the nature of Topper's contract with Children's Television Workshop was also discussed (Harrison Dep., pp. 19-20), together with the means that Topper used to check how Topper's merchandise was moving at the retail level. (Harrison Dep., pp. 20-21)

D 199. Harrison felt that the trade was not correct in its evaluation of Topper. Harrison reached this decision in part on the basis of his conclusion that the trade did not have access to and had not seen the same detail that the Pension Fund had seen regarding Topper, including the Private Placement Memorandum, the Examples of Company's Reporting and the conversations with Downs, Rose and Johnson. (Harrison Dep., pp. 28-29)

D 200. The most time of the August 13, 1971 meeting was spent reviewing the Examples of Company's Reporting (PX 1459). (Thompson Tr., p. 418) Thompson and Harrison jointly looked at practically all of the exhibits in the Examples. (Thompson Dep., p. 186) They specifically looked at the exhibit on accounts receivable, which was prepared monthly and gave a breakdown of aging by current, 30, 60 and 90 days past due. Rose said he was quite proud of the fact that his computer system had helped overcome Topper's past problems. (Thompson Dep., pp. 187-188)

D 201. Topper's June 30, 1971 financial statement showed that as of that time Topper had had sales of approximately $19 million and accounts receivable of approximately $29 million. (PX 1459 at 3,5; ADM 35) Thompson did not try to reconcile these figures. (Thompson Tr., p. 528)

D 202. Topper's June 30, 1971 financial statements showed Topper's sales for the six-month period ended June 30, 1971 to be approximately $19 million. Topper's projected 1971 sales for 1971, as given to Thompson, were between $68 million and $72 million. (Thompson Tr., p. 536; ADM 62-63)

D 203. The analysis of shipments in Topper's June 30, 1971 financials showed a difference of over $1.8 million between gross sales of $21,119,000 and net sales of $19,313,000 for the last six months. (PX 1459 at 24)

D 204. The Examples of Company's Reporting included eight pages of reports entitled "Customer Contract Listing - 08/09/71". Each of these pages showed the account to be "Globe Whse Co. Inc." Seven of these pages made reference to "bill and hold" accounts. (PX 1459 at 261-268)

D 205. One type of report included in the Examples of Company's Reporting was the Credit Summary report which represents the "summary for the day, month to date and year to date of all returns processed by item." (PX 1459)

D 206. Another type of report included in the Examples of Company's Reporting was the Accounts Receivable Report. This report was accompanied by an explanation as follows:

> For the past three years, the Company's accounts receivables have been maintained on the computer with the result that aging of accounts receivable can be prepared quickly after the end of the month, both in summary form by account and in detail for follow-up on collection of open invoices and deductions. In addition, the projection of cash receipts is prepared monthly by the computer indicating anticipated receipts by week. (PX 1459)

D 207. Thompson never asked to see Topper's detailed accounts receivable reports or any other reports, samples of which were in the Examples of Company's Reporting. (Thompson Tr., p. 541; Thompson Dep. pp. 185-188, 454)*

D 208. Thompson believed that the Examples of Company's Reporting indicated that Topper had good controls over its inventories and accounts receivable. (ADM 99)

D 209. At the meeting, Thompson asked Rose to supply him with any later financials on Topper that became available. (Thompson Dep., p. 190) During his investigation, in fact, Thompson asked Rose for later Topper financial figures at least three times, but never received them. (Thompson Tr., p. 525)

D 210. PX 1378 is a memorandum by Thompson concerning the August 13 meeting dictated shortly thereafter. (Thompson Tr., p.418)

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* The last page of each of Topper's monthly aging reports, which Thompson discussed with Rose but did not look at, contains a summary of the agings of all of Topper's receivables. The report for July 31, 1971, for instance, shows over $8 million receivables in the "90-day" column. (PX 352)

D 211. Thompson summed up his feelings in PX 1378 as follows:

> This situation is somewhat offbeat for the Pension Fund but I think that it is quite interesting. The company has the ability to adjust its cost structure rapidly to changing market conditions and appears to be a better credit risk than would be thought for the toy industry. Moreover, management has been uniformly impressive and the basic business appears to be in an uptrend which could prevail for some time. On this basis, we believe that the risk/reward relationship is favorable and that the Pension Fund could invest $3 million in the convertible debenture without undue exposure.

D 212. Thompson was aware, when he wrote PX 1378, that Topper had bank loans of $20.3 million. (PX 1378; Thompson Tr., pp. 528-530)

D 213. The Examples of Company's Reporting which Thompson had reviewed included a copy of Topper's June 1971 financials. Note 1 to these financials stated that Topper's financing arrangement with the Banks provided for maximum borrowings of $18.5 million, of which $18,551,714 were outstanding at June 30, 1971. (PX 1459 at 7) In addition, the April 29, 1971 prospectus stated that "[a]ll loans [under the Financing Agreement] are payable on demand and are made at the discretion of the banks in a maximum available amount (currently not to exceed $18,500,000) . . ." (p. 12) and that there were outstanding bank loans of $19,565,948 (p. 5).

D 214. At lunch after the meeting, Thompson asked Downs what eligible receivables meant. Downs said they were receivables less than 60 days past due. Downs also said that the Lending Banks had all the assets of Topper as collateral for their loans, but that the Lending Banks looked primarily to the accounts receivable. (Thompson Tr., p. 422)

D 215. Thompson kept a copy of the Examples of Company's Reporting after the August 13 meeting and reviewed them further during the following weekend. (Thompson Tr., pp. 537-538)

D 216. Thompson was aware of the percentage of Topper's 1970 sales attributable to the Dawn line and the percentage of Topper's projected 1971 sales attributed to such line. He discussed this with Rose when Thompson received the breakdown of sales by product line. (Thompson Tr., pp. 502-503)

D 217. Harrison, by his August 19, 1971 memorandum to Molé (PX 1411), intended to convey Harrison's approval and his conclusion that Topper was an appropriate investment, and Molé so understood it. (Harrison Dep., p. 57; Molé Tr., p. 700) Molé understood the comparison between the toy and garment business that was mentioned in Harrison's memorandum to mean that the toy industry was very competitive. (Molé Dep., p. 29)

D 218. Neither Thompson nor Molé followed up on the reference in Thompson's August 10, 1971 memo (PX 1373) to Harrison's comment that there were some licensees of toy products who refused to do business with Topper. (Molé Dep., pp. 28-29)

Nelson-Thompson Discussion

D 219. During the week of August 16-23, Thompson discussed the Private Placement with George Nelson, who had retired as a vice-president of the Pension Fund and was a consultant to the Pension Fund. Nelson had done most of the Pension Fund's private placements and had been quite successful. (Thompson Tr., p. 423) Thompson told Nelson that he wanted to make the investment in Topper and asked Nelson's advice on how best to approach Mole. (Nelson Dep., pp. 6-8)

D 220. Thompson told Nelson that he thought the outlook for the toy business was good, that he thought Topper had done a good job with the Sesame Street line and that people thought well of Topper's management. Thompson told Nelson he had checked with Zayre, who thought Topper was competent. (Nelson Dep., pp. 11-12)

D 221. Thompson told Nelson that Citibank was Topper's lead bank and, because of this, Nelson told Thompson to check with Citibank. Nelson also told Thompson that Nelson would check with Glover Johnson. (Nelson Dep., pp. 6, 13-14)

D 222. Nelson felt that Topper constituted a speculative investment for the Pension Fund. (Nelson Dep., p. 19)

Check with White & Case

D 223. Nelson called John McNally, a partner in White & Case, who did all the private placement work for the Pension Fund. He asked McNally if he would ask Johnson what he thought about Topper management and their integrity and whether there were any special problems in Topper that the Pension Fund should know about and how Johnson felt about the general outlook for Topper. Nelson also asked McNally for his opinion of Johnson's judgment. (Nelson Dep., pp. 16-17)

D 224. McNally called Thompson back and told him that Johnson thought Topper management was good, capable and honest, that Topper's outlook was good and that Johnson did not know of any special problems. McNally also said that Johnson was a capable, experienced lawyer-businessman, and that McNally had confidence in Johnson's judgment. (Nelson Dep., p. 17)

D 225. McNally declined Thompson's request that White & Case act as the Pension Fund's "watchdog" in the Private Placement, which McNally understood to be a request that White

& Case underwrite the soundness of the investment. Since White & Case represented Topper as well as the Pension Fund, McNally told Thompson that the Pension Fund was on its own in making its investment decision on the Private Placement. (McNally Dep., pp. 10, 34, 45)

D 226. Thompson received PX 1380 from Rose on August 18, 1971 as a result of a request made by Thompson at the August 13 meeting for any later financial statements after the June 1971 figures and for a "failsafe" calculation indicating at what level Topper could operate and meet the interest payments and sinking fund payments if Topper knew it was going to be a bad toy year ahead of time. (Thompson Tr., pp. 424-425; ADM 85-87)

D 227. Following Molé's return from vacation on August 23, 1971 Thompson gave Mole the memoranda Thompson had prepared on his talks with Cerf, Schwartz, Hessdorf, Folan and Johnson. Molé read these memoranda and the Private Placement Memorandum and discussed them with Thompson. (Thompson Tr., p. 427)

Check with Citibank

D 228. Mole knew that Citibank was Topper's lead bank and that Citibank had a great mass of information about Topper's inventories, receivables, operations and cash flow. Mole told Thompson that with Topper's permission he should contact Citibank. (Mole Tr., p. 662)

D 229. On August 25, 1971 Thompson called Walter Jeffers of Citibank. Jeffers, who was employed in the commercial lending part of Citibank as head of the Metals and Mining Department (Jeffers Tr., pp. 1482-1483), had been handling major corporate accounts in the metals and mining industries, including the United States Steel account, as commercial accounts since early 1970. (Jeffers Tr., pp. 1483, 1485)

D231 Before calling Jeffers, Thompson had written out on a yellow sheet of paper a list of almost ten questions. (Thompson Tr., pp. 431-432)

D 232. Jeffers called Waldman, told him that Thompson of the U.S. Steel Pension Fund had called about Topper and asked Waldman to call Thompson. (Waldman Tr., pp. 1227-1228) Waldman assumed that United States Steel was a large depositor of Citibank. (Waldman Tr., p. 1223)

D 233. Waldman called Thompson on August 27, 1971, saying he was replying to Jeffers' request to call Thompson.* The phone call lasted about five minutes. (Waldman Tr., p. 1229) Thompson told Waldman he was an investment manager at the Pension Fund and was considering an investment in the Topper Private Placement. Thompson asked Waldman what the current size of Citibank's loan was and Waldman said it was several million dollars, that Citibank had a percentage participation in the loan and was lending up to 80 percent of eligible receivables. (Thompson Tr., pp. 433-434)

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*Since Thompson had been told by Orenstein that Waldman was the senior Citibank person on the Topper account, he expected that Waldman would be the one to call him and was not surprised when Waldman called. (Thompson Dep., pp. 61-62)

D 234. Waldman explained to Thompson that Citibank was financing Topper on a commercial finance basis, with loans secured by accounts receivables, inventory, machinery and fixtures. He described the rate of advance against receivables plus, from time to time, against non-receivable collateral. They also discussed the interest rate and the fact that commercial finance loans carried a higher rate because of risks and the work involved. (Waldman Tr., p. 1228) There was no discussion of Topper's financial condition or whether there were any problems in connection therewith. Waldman did state that there were no problems in Citibank's relationship with Topper. (Waldman Tr., p. 1270; PX 1379)

D 235. In response to Thompson's questions, Waldman gave honest answers. (Court Tr., p. 1455)

D 236. Thompson's phone conversation with Waldman concerning Topper was a credit check. (Lang Dep., pp. 18-19; Molé Dep., pp. 51-52, 92-93; Nelson Dep., p. 14; PX 1407; HSX Molé G14; HSX Molé G15; PX 1370; PX 1396B)

D 237. A credit check in the course of the investigation of an issuer by the Pension Fund was standard practice and was appropriate in the case of the Private Placement. (Van Deusen Dep., pp. 16-17; Nelson Dep., p. 31; Lang Dep., pp. 72-73; Thomas Dep., p. 30; Walker Dep., p. 29) The Pension Fund would have made such check with whatever bank handled

Topper's loan. (Van Deusen Dep., pp. 16-17; Walker Dep., pp. 30-31; Lang Dep., pp. 17-18)

D 238. Thompson's telephone call with Waldman was a request for information, not advice,on Topper. (PF Ans. 7(C), 11(d) - (e) to HS Interrogs. 7, 11; Thompson Tr., pp. 431-432; Waldman Tr., pp. 1258-1259; PX 1410) Consistent with this fact, Waldman specifically declined to answer Thompson's question whether Topper was a good investment for the Pension Fund. In fact, Waldman ducked this part of Thompson's inquiry. (PX 1379; Thompson Dep., pp. 29-31) Similarly, Molé told Thompson it was inappropriate for Thompson to have asked Waldman whether the Pension Fund should invest in the Private Placement. (Molé Tr., pp. 702-703, 716-717; Molé Dep., p. 151)

D 239. Jeffers and Waldman treated Thompson's phone call as a routine credit inquiry. (Jeffers Tr., pp. 1493-1494) Waldman's conversation with Thompson was consistent with Waldman's and the Hubshman Factors Department practice followed with respect to inquiries respecting clients of the department. Department practice was to describe the security and the appropriate amount of the advance and to state whether the relationship was satisfactory. (Lusk Tr., p. 1014; Siegel Tr., p. 1131; Waldman Tr., pp. 1220-1230) It was normal practice to give out such information on the department's clients to institutional inquirers without specific authority from the client. (Waldman Tr., pp. 1229-1230)

D 240. Shortly after his conversation with Thompson, Waldman received a call from Provine, at White & Case. Provine, who Waldman knew to be Topper's lawyer, told Waldman that he would be hearing from a Mr. Thompson concerning the Pension Fund's investment in Topper. Waldman told Provine he had already talked with Thompson. (Waldman Tr., pp. 1230-1231)

D 241. Immediately following his conversation with Waldman, Thompson dictated PX 1379 from the notes he had taken during the conversation (Thompson Tr., p. 447)* and gave a copy to Molé. (Molé Tr., pp. 701-702)

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*Thompson's contemporaneous memorandum concerning his phone conversation with Waldman describes his only discussion of "problems" as follows:

> "The relationship between FNCB and Topper has been good and there are no problems at the moment nor does Mr. Waldman anticipate any." (PX 1379)

In his deposition, however, Thompson stated as follows:

> "I asked Mr. Waldman how Topper had performed in the audits and he indicated that Topper had performed well in the audits, and that there were no problems.
>
> . . .
>
> The next question, I remember very vividly, it was, are there any current problems in Topper?
>
> Mr. Waldman responded with one word, No.
>
> I paused to let him add anything that he might want to add, and he didn't add anything.
>
> The question after that, do you anticipate any problems in Topper?
>
> . . .

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* (Cont'd from p. 90)

> Again he replied No. One word. I paused . . . in case he wanted to add anything to it. He did not make any qualifications.
>
> So then . . . I am distinct on this because in dictating the memo I had these two questions with the one-word answers, and I remember pausing to see if he wanted to add anything to his statement or, in any way qualify it, and he did not." (Thompson Dep., pp. 20-22)

Third, in his direct trial testimony, Thompson recounts the "problems" discussion as follows:

> "Well, the next one was, 'How has the company performed in these audits? Are there any problems that you see in the current financial condition of Topper?'
>
> Q Let us stick to the first part of that, 'How does the company perform the audits?' What did you mean?
>
> A I really meant what I asked in the second part. I had written down on the paper to specifically ask, you know, what is the current financial condition of Topper, and Waldman's response to my first question led into that second question, and that is what we then discussed. (Thompson Tr., pp. 435-436)
>
> * * *
>
> Q Go ahead. In response to your question as to how the company had performed, were there any current financial problems, what did Mr. Waldman say?
>
> A He said there were none. He said, 'Nothing showed up in the audit of receivables.' (Thompson Tr., p. 436)
>
> * * *
>
> So the thrust of these questions was to get assurance that, you know, there were no problems that Waldman knew of in the financial condition of the company.
>
> Q Or to learn from him what the problems were, if there were any?
>
> A Exactly. (Thompson Tr., p. 436)
>
> * * *

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* (Cont'd from p. 91)

Q You asked Mr. Waldman if there were any problems. What was his response?

A Well, I mean I covered these two points that had come up in discussion with Mr. Mole, and I think at that point I asked whether there was any problem that had come up in these audits of receivables.

Q What was Mr. Waldman's response?

A There were no problems in the audits of receivables, and so I covered these two points and then I went on to this general question, 'Are there any current problems in Topper?' to which he replied, 'No.' And I gave a pause and gave him a chance to add any information or to qualify it. And then I went on to ask him, 'Do you anticipate any problems in Topper?' And here again he replied, 'No.' And when I dictated this memorandum, which was right after the conversation, I had this right in front of me and just turned around and put it in the memo. . . . I just don't see how he could say that there were not any problems in the audits of receivables when later on we found -- . . . . (Thompson Tr., pp. 442-443)

He was aware that Orenstein's pet Sesame Street toy was the Spell-O-Phone, and that others in the company had developed toys which I think we both thought were more interesting, namely, Walking Letters was one that we discussed, and he was also aware that Orenstein was checking with the trade to see how the Dawn program was doing and how the other Topper products were doing, and at this point I asked him if the bank in connection with its audits made any independent checks in the trade to, in effect, confirm what Orenstein was telling them, and he said, yes, they did.

And I asked him whether there were any problems or anything came up in those checks that was negative, and he said nothing came up. (Thompson Tr., p. 445)

* * *

Inglis called up to find out how the information that I had gotten from the bank turned out and I don't remember the exact details of the conversation because he was asking me questions and I was replying to him, but I did tell him that there weren't any problems in the audits of receivables that the bank was doing and that we had received favorable information from them, that they viewed the company's management as competent and the controls good and that they didn't know of any problems in the situation currently." (Thompson Tr., p. 449) (Emphasis added.)

September 1 Meeting

D 242. On September 1, 1971, Thompson and Molé held a meeting in Molé's office with Inglis, Orenstein, Downs and Rose, as Molé had not yet met Topper management. (Thompson Tr., pp. 549-550) Orenstein and Downs stated that the Dawn program had been a success. Orenstein said that Dawn merchandise had been purchased for a similar program in December 1971 and to replace Dawn merchandise that had been sold. Orenstein was even more enthusiastic than were Hayden Stone's budget figures and the Rose sales figures in PX 542, and said that Topper in 1971 would probably do three or four million dollars in sales above the $68 million sales projection. Also

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* (Cont'd from p. 92)

In his memo of January 3, 1974 to Mr. Lang (PX 1401) on the subject of "Topper's Receivable and Inventory Problems and Representations to U.S. Steel Pension Fund", Thompson recounts the phone call as follows:

> ". . . Waldman called me on August 27, 1971 and told me among other things that there was no problems, he did not anticipate any, Rose was a competent financial officer and that Topper had shown itself to be competent in the bank's audits."

In yet another version, Thompson described the conversation as follows:

> ". . . I remember telling [Inglis] that the check with First National City Bank had been favorable and that we had been told that there weren't any problems in Topper; that Mr. Rose was a competent financial person; that the bank worked closely with his staff and that the bank did not know of any problems in the receivables and that the company had performed well in the audits." (Thompson Dep., p. 230)

discussed was the closeness of the Topper - Hayden Stone relationship and the fact that two of Hayden Stone's senior partners, Berlind and Weill, were on Topper's Board of Directors, that they had their own money invested in Topper and that Hayden Stone's profit sharing plan invested money in Topper. (Thompson Tr., pp. 450-452)

D 243. Mention was made again that Orenstein was monitoring the flow of Topper merchandise at key retail outlets. Orenstein said that the Smarty Pants doll was likely to be the doll of the season. He was also enthusiastic about the Sesame Street line and said he thought Topper would do about $21 million in sales in Sesame Street products in 1971. (Thompson Dep., p. 206)

D 244. Molé, very conscious of Topper's past history, asked whether the practice of selling on consignment had been abandoned and asked about Topper's past period of substantial losses. Everyone at the meeting assured Mole that the consignment practice no longer existed and that sales were final sales. (Thompson Dep., p. 207; 474; Molé Dep., p. 58)

D 245. PX 1459, the Examples of Company's Reporting, was reviewed again. Orenstein and Rose made reference to the reports of which samples were in PX 1459. (Thompson Tr., p. 452)

D 246. Molé asked Downs about Topper's relationship with Manufacturers Hanover. Downs said he did not know of anything that was wrong, that it was a good relationship and that Manufacturer's Hanover had a favorable opinion of Topper. (Thompson Tr., p. 452; Molé Dep., pp. 62-63)

D 247. Following the September 1 meeting, Thompson prepared PX 1370, a decision memorandum to the Pension Fund committee of finance. (Thompson Tr., p. 453) The decision memorandum contained the following last paragraph:

> "Our retail trade and banking checks have been favorable and this issue provides us the opportunity to obtain an interesting, though admittedly offbeat, participation in a seemingly well-managed company in a growing phase of the economy. Accordingly, it is recommended that we purchase $3.0 million of the Topper convertible debentures in view of the high expected payoff, if the company is successful in quadrupling earnings per share in the next four years and increasing stability of the toy industry and of Topper, in particular."

The mention of "retail trade and banking checks" in the last paragraph of PX 1370 refers to Thompson's discussion with J.C. Penney and Zayre, his conversation with Waldman and Downs' reference to Manufacturers Hanover. (Thompson Tr., p. 554)

D 248. Thompson discussed his phone conversation with Waldman with Inglis "a few days after the September 1 meeting with the Topper people" (Thompson Dep., pp. 541, 230) or "the day [he] prepared the memorandum to the Committee on Finance dated September 2, 1971, or within a few days afterwards" (Thompson Dep., p. 542) or sometime between August 30, 1971 and the end of that week. (Thompson Tr., p. 449)

D 249. Prior to the Private Placement, Thompson did not review the Financing Agreement or the Ford Motor Credit agreement. (Thompson Tr., p. 533) He did review the Ford commitment letter and knew that the Ford Loan was to be secured and that it carried a maximum interest rate of 14 per cent. (Thompson Tr., pp. 556-557; ADM 41, 53)

D 250. Thomas Ramseur, who was the White & Case partner in charge of representing the purchasers in the Private Placement, knew that there had been a temporary increase in the Lending Banks' line prior to the Private Placement. (Ramseur Dep., pp. 141, 186-187, 190, 235) The Private Placement Purchase Agreement (PX 1369) stated that:

> "... The copies which the Company has furnished to you of the Company's ... loan agreements are complete and accurate and include all amendments thereto."
> (p. 5, ¶5.5)

D 251. The mention of "retail trade and banking checks" in the last paragraph of PX 1370 refers to Thompson's discussion with J.C. Penney and Zayre, his conversation with Waldman and Down's reference to Manufacturers Hanover. (Thompson Tr., p. 554)

D 252. Thompson was given full access to Topper's records and was free to check anything he wanted to check. (Orenstein Dep., pp. 446-448; Inglis Dep., pp. 88-89)

D 253. In total, Thompson spent 60 to 80 hours investigating the Private Placement, not including time spent analyzing the investment apart from the preparation or review of documents and in certain telephone conversations the duration of which cannot be estimated. (PF Ans. to Orenstein Interrog. 1-3)

D 254. In October 1971, Thompson received Topper's financial statements for the nine months ending September 30, 1971. Upon reading these statements, Thompson concluded they showed Topper to be a soundly financed company with improving earnings. (Thompson Tr., p. 560; PX 1390 at 2; ADM 102)

D 255. On or about January 3, 1974 Thompson sent Lang a memorandum entitled "Topper's Receivable and Inventory Problems and Representation to U.S. Steel Pension Fund." (PX 1401)

D 256. In PX 1401, Thompson stated that he was alerted to investigate problems in Topper's receivables and inventories for the following reasons:

> 1. Hayden, Stone sent us a preliminary prospectus in connection with Topper's June 1970 common stock sale that included a past history of substantial deficits and included history of the buy-back from Philadelphia & Reading of the company by Henry Orenstein. We had no interest in this offering because of Topper's past record and highly leveraged capitalization.
>
> 2. The private placement brochure for the subordinated convertible notes supplied to us by Hayden, Stone about fifteen months later in late July 1971 or early August, contained a prospectus

of Topper's April 1971 public common stock financing. It again mentioned the substantial losses in Topper's past. At one point, it said losses in 1966 were in part caused by "liquidation of large quantities of inventories at substantially reduced and close out prices." A few pages later, the prospectus indicated Henry Orenstein and his uncle Marrius had introduced a selling program through supermarkets "which permitted retail outlets to return unsold merchandise for sale during Christmas 1953." This prospectus also made reference to Topper's December 1970 $14.0 million Spring Program, consisting largely of "Dawn" dolls and clothing, on which payments were due five to eight months later in May to July 1971.

3. The Topper 1970 Annual Report, whose financial statements were certified by Arthur Young & Co., was supplied to us in August 1971. In a footnote, it also referred to the December 1970 $14.0 million Spring sales program. The footnote entitled "Accounts Receivable" reads as follows:

> "Approximately $14.0 million of sales made in December 1970 carried extended credit terms of five to eight months. The comparable amount for the prior year was $2.0 million."

4. In a conversation on August 12, 1971 with Glover Johnson, a partner in White & Case and director of Topper, he said that Topper had been forced by Philadelphia & Reading to sell on consignment when it was part of that company. He said that this practice had been discontinued after Orenstein's repurchase of the company, which he had helped to arrange. In fact, however, the company had sold a substantial amount of merchandise to certain customers under secret agreements which provided for exchange and return of the merchandise.

Previously, Mr. Johnson had called me to recommend Topper as an investment for the Pension Fund in connection with the June 1970 common offering. Remembering this in early August 1971 and knowing that White & Case was Topper's general counsel, I called Jack McNally at the beginning of my investigation of the private placement and asked about the integrity of Topper's management. He replied that he believed that all of White & Case's clients were honest and that his firm could not provide us with information on Topper because of its being the company's general counsel. Even so, Glover Johnson volunteered through Orenstein to provide us with any help that he could on Topper and thus I spoke to him upon his return from vacation on August 12, 1971.

D .257. Thompson stated in PX 1401 that the following inquiries were made and assurances received concerning Topper's receivables and inventory:

1. On August 4, 1971, I spent the day on a Hayden, Stone arranged trip of Topper's New York showroom and Elizabeth, New Jersey plant and headquarters. During the course of my visit:

a. Mr. Orenstein indicated that he personally monitored the over-the-counter sale of toys at key outlets, that merchandise was moving very well, that the business of his company was more stable than that of the industry because Topper's line contained many lower priced, more stable toys and that the "Dawn" doll line was doing particularly well against Mattel's "Barbie."

b. Mr. Rose said that past billing problems had been corrected, that bad debts on accounts receivable were small and should be under $200,000, that sales were final sales and were not returnable, and that the company was "hardnosed" on its return policy. He also indicated that Topper had an elaborate computer system to prevent over-ordering of inventory and to keep track of receivables, and that major new capital expenditures for molds and parts were not made until management was sure goods were moving in stores, and that the credit department of Topper regularly asked customers about how toys were selling.

c. I was introduced by Orenstein to someone at the Topper headquarters who showed me Polaroid snapshots of "Dawn" displays taken in stores by Topper salesmen. This was said to be used by management as a means of knowing inventory levels in stores and was cited as proof that the company knew its "Dawn" line was selling well. It was "Dawn" merchandise that comprised much of the $14.0 million December 1970 shipments.

d. Jay Inglis of Hayden, Stone said his firm was quite close to Topper, that Topper was Weill's and Berlind's largest personal holding, that his firm had been the investment banker for several financings over the past few years and that Topper's former problems had been corrected. He also indicated that Topper's merchandise was selling well and that the company's business was relatively stable with below average dependence upon Christmas.

2. On August 17, 1971, Rose and Downs of Topper met with Mr. Harrison and me at our offices for over two hours. Rose cited the company's excellence in avoiding inventory control problems, its day-to-day checks at this time of year on the movement of product in stores, Topper's elaborate computer based control system, and its ability to defer capital investment until it had a good reading of customer response to new products. Downs emphasized the stability of the product line and the success of the relatively low priced "Dawn" line.

3. At the above meeting, Rose provided a booklet entitled, "Examples of Company's Reporting." This booklet had exhibits and brief write-ups supporting Rose's statements about good control of inventories and receivables including an analysis of orders and shipments, sales analysis reports, a credit summary and an accounts receivable report.

4. At this same meeting, I asked Rose about Topper's breakeven sales point and he sent a "fail-safe" calculation showing that his company could successfully cover interest and sinking fund payments on all debt including our private placement at a volume level of $39.0 million in 1972 compared with a sales projection of $68.0 million for 1971. The letter added, "The decision to operate on a "fail-safe" basis is made in the Fall of the prior year. We believe that any extraordinary weakness in any of the company's products would be known to us in the Fall."

> 5. On September 1, 1971, Orenstein, Rose, Downs, and Inglis visited Mr. Mole and me at our offices mentioning among other things the success of the "Dawn" line and the improved stability of the product line. Mr. Mole is not sure whether it was at this meeting or not, but he recalls discussing Topper's past problems and receiving assurances that the computer system would prevent their recurrence.

D 258. In addition, Thompson stated in PX 1401, he made "these further checks" with White & Case, Zayre, J.C. Penney and Waldman:

> 1. Towards the end of August and after my conversation with Glover Johnson, George Nelson at my request contacted Tom Ramseur and/or Jack McNally of White & Case and asked them about Glover Johnson. I was told by Mr. Nelson that Johnson was well regarded, that he was still considered to possess good judgment at about age 70, and that he was thought within White & Case to be interested in this type of company and to have had past success in his personal investments.
>
> 2. I contacted Sumner Feldberg, then executive vice president and now president of Zayre, whom I knew through the Pension Fund's investment in his company, early in August after my visit to Topper's headquarters. He placed me in touch with Mr. Hessdorf, the Zayre toy buyer, on about August 11, 1971. Mr. Hessdorf said he knew Henry Orenstein well and that Zayre did considerable business with Topper. He made no mention of the right to return or exchange merchandise, or any special arrangements on such matters between his company and Topper.
>
> 3. Likewise, early in August after my visit to Topper's Elizabeth facilities, I telephoned John Hebard, assistant treasurer of J.C. Penney, with whom I had previously completed a $7.4 million sale-leaseback, and requested to speak with his firm's

> toy buyer who knew Topper. Pursuant to this request, I talked on about August 11, 1971 to a Mr. Folan, who indicated that J.C. Penney's business with Topper had increased in each of the past six years and that he was satisfied with his relations with Topper. Like Hessdorf, he made no mention of right of return or exchange for merchandise.

Knowing of Topper's factoring arrangement with First National City Bank, I was told by Orenstein that I was free to check with Edward Waldman, whom he said was the senior man on the account. In response to an inquiry I made to Walter Jeffers, Waldman called me on August 27, 1971 and told me among other things that there were no problems, he did not anticipate any, Rose was a competent financial officer and that Topper had shown itself to be competent in the Bank's audits. Subsequently, we learned, among other things, that the First National City Bank knew that past due accounts receivable had increased substantially in July and August 1971 and that this trend continued in September.

Subsequent Memoranda

D 259. A memorandum of John G. Van Deusen, a Vice President - Investments of the Pension Fund, dated December 29, 1971 (PX 1389) stated that the Pension Fund "would not directly ask the banks to repay [it]."

D 260. A memorandum of Henry L. Thompson dated January 3, 1972 (PX 1400) stated that "[i]f there is a bankruptcy in this instance, FNCB could be placed in the position of having to defend itself concerning mismanagement of the account and would at least be subjected to adverse publicity if its dealings with [the Pension Fund] were known." (PX 1400, ¶ 7)

D 261. A memorandum of Harvey Molé dated January 19, 1972 (PX 1482) stated that Molé "was quite certain that [Citibank] had not foreseen the extent of Topper's problems...." (Tr., p. 688)

D 262. A memorandum of Harvey Molé dated February 16, 1972 (PX 1479) stated that it was the Pension Fund's "point that Mr. Waldman had given [it] substantially less than full disclosure" and that Molé did "not believe that Mr. Waldman had any inkling that the company would get into difficulties within three months' time [when he talked to Thompson]." (Tr., p. 694)

D 263. A memorandum of John G. Van Deusen dated February 23, 1972 (PX 1413) stated that the Pension Fund's "complaint is mainly for what [Waldman] did not say."

D 264. A memorandum of Henry L. Thompson dated August 16, 1972 (HSX Molé G15) stated that

> "In view of the present status of Topper, we have reviewed our legal position with Winthrop, Stimson, Putnam and Roberts with respect to instituting an action against FNCB for its failure to provide full disclosure in our credit check and the subsequent use of our money to reduce its loan balance. We have been told that litigation against FNCB could last for years and that it would be

> expensive. Moreover, our case would be difficult to prove since our evidence would have to be supplemented by additional facts brought out in the pre-trial discovery process and through cross-examination. Accordingly, Winthrop, Stimson believes that the outcome of litigation against FNCB is too uncertain to justify the time and expense involved."

(HSX Molé G15 at 2)

D 265. Memoranda of Henry L. Thompson dated February 13, 1973 (PX 1408) and February 22, 1973 (PX 1390) characterized the Pension Fund's complaint against Citibank as "the lack of disclosure by Mr. Waldman." (PX 1408 at 2; PX 1390 at 2)

D 266. A memorandum of W.H. Lang of the Pension Fund dated November 8, 1973 (PX 1410) stated that

> "While it was no secret that the Pension Fund investment was to be used as a reduction in the FNC loan, the combination of the failure of the company within sixty days after October 1 and the extension of the loans made it appear obvious to us that we had not received proper service and that the bank bore responsibility."

VI. Background to Custodian Agreement

D 267. The only contractual relationship between the Pension Fund and Citibank was that which existed under a letter agreement dated November 30, 1950 (CBX 12), as amended by a letter agreement dated April 3, 1959 (CBX 13) and as amended from time to time by letters which revised the applicable fee schedule including a letter dated April 6, 1960 (CBX 159), together known as the "Custodian Agreement." (PF Ans. 7A to HS Interrog. 7)

D 268. The 1960 letter amendment to the Custodian Agreement read as follows:

> "Commencing with an agreement dated November 30, 1950 we have acted as custodian for the assets of the United States Steel & Carnegie Pension Fund at a scale of fees which has been adjusted from time to time as the growth of the Fund and other considerations warranted. The agreement itself has been amended from time to time and the one now in effect, under which we are operating, is dated April 3, 1959. After due consideration of all the circumstances and a further study of our operating costs, we think it would be fair and equitable to change the present fee schedule as it was fixed by letter agreement of July 16, 1956 so that commencing January 1, 1960 our compensation for acting as custodian in accordance with the custody agreement dated April 3, 1959 will be:
>
> "1/100ths of 1% of the value of the Fund from time to time.
>
> "The terms of the amended agreement dated April 3, 1959 will remain in full force and effect, except insofar as they may be affected by the change in compensation hereinabove provided.

> "If the foregoing meets with your approval, please be good enough to sign and return the enclosed copy of this letter, which will then constitute an agreement between us."

D 269. Citibank was a "joint custodian" with Morgan Guaranty or its predecessor of the assets of the Pension Fund's non-contributory pension trust, which represented about 90% of the Pension Fund's assets, at the time the Custodian Agreement was entered into. (Molé Tr., pp. 636-637) The relationship between the Pension Fund and Morgan Guaranty existed under a letter agreement dated November 30, 1950 (CBX 56), as amended by a letter agreement dated April 3, 1959 (CBX 57), which apart from the names of the custodians are identical to the letter agreement and amendment thereto between the Pension Fund and Citibank of the same dates. (CBX 12-13, 56-57)

D 270. Pursuant to the Custodian Agreement, Citibank registered securities, collected and credited income with respect to the securities held in the custodial account, handled the redemption and delivery of securities and credited the proceeds thereof, exchanged temporary for permanent securities and performed other custodial services with respect to the securities held in the custodial account. (ADM 256; CBX 12-13)

D271. Under the Custodian Agreement Citibank was not empowered to exercise its own discretion in the investment of any assets of the Pension Fund. (PF Ans. to HS Interrog. 11(b))

D272. In addition to providing for numerous duties of a custodial or administrative nature, the Custodian Agreement, prepared by the Pension Fund, provided as follows:

> "You [Citibank] agree to provide the undersigned [the Pension Fund] with investment advice with respect to any government bonds or other securities held from time to time in the custodian account or with respect to any cash held by the undersigned for investment."

(CBX 12 at 2; CBX 13 at 1) The agreements between the Pension Fund and Morgan Guaranty contained identical language, pursuant to which Morgan Guaranty from time to time rendered "investment advice" to the Pension Fund. (CBX 56-57; Molé Tr., p. 636)

D 273. The funds used for the purchase by the Pension Fund of $3 million notes in the Private Placement were taken from thePension Fund's custodial account with Morgan Guaranty. (CBX 58-59)

D 274. Citibank's rendering of "investment advice" under the Custodian Agreement consisted only of "four meetings a year of four or five of [its] Senior Investment Officers with the investment officers of the United States Steel Pension Funds". (CBX 64 at 2)

D 275. At the quarterly meetings Citibank and the Pension Fund discussed investment policy on publicly traded securities, what percentage of Citibank's holdings was in equities, what percentage was in bonds, long and short term, what it thought of the bond market, the equity market. These discussions related almost entirely to public securities, except that the Pension Fund occasionally asked whether Citibank was purchasing securities in private placements as well. (Molé Tr., p. 644; CBX 146-150, 154)

D 276. Aside from the investment advice rendered by Citibank at the quarterly meetings, the Pension Fund personnel on occasion would make inquiry concerning matters or clients with respect to which various persons at Citibank had expertise. (Molé Dep., pp. 642-643) Such discussions were never cast in the form of recommendations that the Pension Fund buy, hold or sell a specified number of shares or other securities of a particular corporation; but consisted merely of responses from Citibank to a particular request for information from persons in the commercial or credit area of Citibank believed to possess particular expertise concerning the specific subject matter of interest to the Pension Fund. (PF Ans. to HS Interrog. 11(d)-(e); PF Ans. 7(C) to HS Interrog. 7;

Molè Tr., pp. 642-644, 646, 669; Molè Dep., pp. 95-105, 205-206)

D277. With respect to proposed private placements of securities, as distinguished from publicly traded securities, the Pension Fund relied more extensively on information from outsiders of the issuer who had particular knowledge of the issuer, such as an underwriter or investment banker or competitor of the issuer. (Molè Tr., pp. 644-645; Thompson Tr., pp. 382-383) Topper's stock was publicly traded on the American Stock Exchange at the time of the Pension Fund's investigation of Topper, and a current registration statement was available. (PX 690; Lusk Tr., pp. 1065-1066)

D 278. The occasions on which the Pension Fund requested information of Citibank concerning particular matters included: (i) several tanker financings, approximately during 1958 to 1961, for which information the Pension Fund consulted Carl Wedel, head of Citibank's Tanker Loan Division; (ii) a loan to Kerr-McGee, approximately in 1960, for which information the Pension Fund consulted Bob Hoguet, a senior vice president of Citibank; (iii) a loan to Drew Chemical Company, approximately in 1964 or 1965, for which information Nelson of the Pension Fund consulted Howard Miller of Citibank; (iv) numerous oil investments, including Goliad, a Canadian oil investment, Dora Roberts, a Texas oil payment, and Ventura, a California oil payment, from approximately 1955 to 1962 or 1963, for which information the Pension Fund used Charlie Dodson of Citibank to obtain engineering estimates; (v) an electronics subsidiary of Phillips Lamp, approximately in the late 1960's, for which information was obtained from Citibank by John Van Deusen of the Pension Fund; (vi) Trice Production Company, a loan on some oil properties, approximately in 1960, for which information the Pension Fund consulted Scott and Spencer of Citibank and were told that it was a sound investment, but subsequently decided not to invest because of the company's poor financial condition; and (vii) Beverly Enterprises, a private placement which Citibank brought to the attention of the Pension Fund, in 1969, in which the Pension Fund decided not to participate. (Molė Tr., pp. 646-647, 713-714; Molė Dep., pp. 97-105, 205-206; Thompson Tr., pp. 384-387) None of these Citibank-Pension Fund contacts, therefore, had taken place after 1969.

D 279. On those occasions when the Pension Fund requested information from Citibank about an issuer Citibank either had or had had a loan outstanding to such issuer; Citibank did not make any investigation into any such issuer for the purpose of giving information to the Pension Fund apart from any investigation which it had made for its own purposes and any such information given the Pension Fund had already been compiled by Citibank. (Mole Dep., pp. 100-103; Mole Tr., p. 714)

D 280. On certain occasions during the term of the Custodian Agreement the Pension Fund contacted Citibank "to inquire whether the bank was interested in participating in a private placement that U. S. Steel was participating in." (Mole Tr., pp. 715-716)

D 281. In answering Thompson's questions concerning Topper in the course of Thompson's telephone call with Waldman, Citibank did not act pursuant to the Custodian Agreement.

D 282. In the case of a call such as Thompson's inquiry on Topper,, it was normal practice in the commercial banking sectors of Citibank for the Citibank individual called to contact the Citibank person handling the account in question and ask him to phone the person inquiring to see if he could provide information to him. Citibank personnel tought of this type of inquiry as a credit inquiry, since it had long been strong Citibank policy that commercial lending officers could not give any investment information or advice to anyone. (Jeffers Tr., pp. 1493-1494, 1500)

D 283. In answering Thompson's questions concerning Topper in the course of Thompson's telephone call with Waldman, Citibank did not recommend that the Pension Fund participate in the Private Placement; nor did Citibank purport to give investment advice to the Pension Fund.

VII. Connecticut Mutual Investigation

D 284. Hieronymus worked as a securities analyst with Mutual of New York for five years before joining Connecticut Mutual. (Hieronymus Tr., p. 616)

D 285. Hieronymus obtained a masters degree in Business Administration from New York University in 1971. (Hieronymus Tr., p. 571)

D 286. In mid-July 1971, Weir told Hieronymus he had received the Private Placement Memorandum from Inglis, asked Hieronymus to read it and set up figures to see if the Private Placement was something Connecticut Mutual might be interested in. (Hieronymus Tr., p. 574; ADM 151)

D 287. Following his review of the Private Placement Memorandum, Hieronymus prepared a summary sheet listing Topper's sales, income, fixed charges, interest charges, net income and earnings per share. On a balance sheet form, Hieronymus listed items such as net working capital and capitalization, including debt and shareholders' equity. He also calculated the amount of funded debt to total capitalization. Hieronymus prepared these figures in order to put Topper in a standard format in which it could be analyzed in comparison with a lot of other deals Connecticut Mutual had been working on. (Hieronymus Tr., p. 576; ADM 153)

D 288. Hieronymus asked Inglis to send him Topper's latest financial statements and a list of Topper's ten largest customers. Rose sent Hieronymus PX 1420, a letter dated August 9, 1971, enclosing Topper's six-month unaudited financials and a list of Topper's ten largest customers. (Hieronymus Tr., p. 577; ADM 155, 158)

D 289. From the Private Placement Memorandum and Topper's June 30, 1971 financials, Hieronymus knew that Topper's reported sales year to date as of June 30, 1971 were $19 million, that its accounts receivable as of June 30, 1971 were over $28 million and that its projected 1971 sales were $68 million. (Hieronymus Tr., p. 620)

D 290. After he had reviewed Topper's six-month financials, Hieronymus had a second meeting about Topper with Weir, at which he discussed some of the points he thought were important: that there had been an increase in Topper's sales in the past few years, that Topper's new products introduced in 1971 had been well received, that Topper had received a contract from Sesame Street. Hieronymus felt these were favorable factors indicating that Topper was gaining momentum. (Hieronymus Tr., p. 578; ADM 156)

D 291. Inglis told Hieronymus that "a major fund" had investigated Topper, had visited Topper's facilities and was very impressed with Topper's management and products. Inglis suggested that Hieronymus visit Topper. (Hieronymus Tr., pp. 579-580)

D 292. Prior to his trip to Topper, Hieronymus asked Inglis in a phone conversation about the possibility of the Lending Banks going unsecured. Hieronymus felt that in the usual case where junior money was coming in, there was an additional equity as far as the secured lenders were concerned, and often the secured lenders, seeing a stronger financial situation for the company, will go on an unsecured basis. Inglis undertook to find out what the Lending Banks' situation was. (Hieronymus Tr., pp. 585-586) During his trip to Topper, Hieronymus was told by Downs that the Lending Banks had agreed to review Topper's loan in the Spring of 1972 with a view toward changing the loan to an unsecured basis. (ADM 143)

D 293. Hieronymus started his August 11, 1971 visit to Topper first thing in the morning at Topper's New York City showroom, where he met Inglis, Orenstein and Downs. They reviewed the various Topper toy exhibits, including Dawn, Ding-A-Lings, Johnny Lightning, Suzie Homemaker and Sesame Street. Orenstein stated that Dawn was doing very well, with $30 million in sales already in hand, and that with the orders Topper had received it looked like the $68 million in sales that Topper had projected in 1971 was going to be exceeded. Orenstein said he had never been wrong in his analysis of the projections this late in the year. (Hieronymus Tr., pp. 580-581)

D 294. Orenstein told Hieronymus that new orders of Sesame Street products, mainly Muppets, had been well received, and that he had several other Sesame Street products that had already been approved and would soon be on the market. Orenstein said that these Sesame Street items were very favorable to Topper, would sell on a year-round basis, have an educational benefit and give stability to Topper. (Hieronymus Tr., pp. 581-582) Hieronymus believed that Topper's products "Walking Letters" and "Spell-A-Phone" could easily do $20 million per year in volume of sales. (PX 1417 at 2; ADM 141)

D 295. From Topper's showroom, Hieronymus, Inglis, Orenstein and Downs went to Topper's plant in Elizabeth, New Jersey. During the trip Orenstein explained the history of Topper and how he and others came to purchase Topper from Philadelphia & Reading in 1966. Orenstein explained how at the time of the repurchase Topper was experiencing severe losses because of an inventory pile-up. He said one reason for the pile-up was a bill-and-hold policy Orenstein had instituted, and that due to the bad experience he had had with this policy, all sales were now on a final basis. (Hieronymus Tr., pp. 583-585; ADM 144)

D 296. Downs, who said that he used to work at Manufacturers Hanover, suggested that Hieronymus contact the banks and Orenstein said that would be a very good idea. Hieronymus was given the names of individuals at Citibank and Manufacturers Hanover whom he could contact. Hieronymus wanted to get from the banks an idea of how they felt about Topper management. (Hieronymus Tr., pp. 585, 595)

D 297. Upon arrival at Topper's plant, Hieronymus toured several areas, including the product testing area, where Sesame Street toys were being tested, and the graphic arts area, where designs for promotional displays were being made. Hieronymus talked to a Topper employee who was costing Topper's products and determining what each item in the manufacturing process and overhead cost. (Hieronymus Tr., p. 587)

D 298. Following lunch, Downs took Hieronymus on a tour of Topper's manufacturing facilities. (Hieronymus Tr., p. 588)

D 299. Hieronymus then toured Topper's computer room and discussed several things concerning accounting, controls and various programs that Topper had computerized. Hieronymus saw a run of orders which totalled $53 million. He asked Rose if these orders were good, in order to verify that Topper's past bill and hold practices were not being used again and that there would be ultimate sales that would not become inventory if they were not sold. Rose responded that Orenstein thought they were good orders and that Orenstein, to Rose's experience, was never wrong this late in the year. (Hieronymus Tr., pp. 589-591; ADM 145, 164; Hieronymus Dep., pp. 34-35)

D 300. Hieronymus was interested in finding out whether the receivables from the $14 million sales on an extended dating basis in 1970 had actually been collected. Since they were then well into August and the extended dating receivables were on a five to eight month basis, Hieronymus asked Rose if they had been substantially collected. Rose did not respond. Upon repetition of the question, Rose told Hieronymus that such receivables had been substantially collected and that Topper was not experiencing any delinquencies on them.* Rose said that if Topper went out of business, these receivables could all be collected. Rose added, however, that as a matter of good will, Topper usually had an allowance of five to seven percent on exchanges of material that customers might send back. (Hieronymus Tr., pp. 591-593; Hieronymus Dep., p. 35)

D 301. When Rose told him that the extended dating receivables had been substantially collected, Hieronymus had read the June 30, 1971 Topper financials and knew that as of June 30, 1971, Topper had $19 million sales year to date and $28 million of outstanding accounts receivable, or an excess of $9 million accounts receivables over 1971 sales. (Hieronymus Tr., pp. 616-617)

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*In his deposition, Hieronymus described the conversation as follows:

> "I asked Mr. Rose since it had been almost eight months since the time in which the sales were made back in September (sic), weren't these receivables all collected. And Mr. Rose at that point asked to have the question repeated and Jay Inglis at that point repeated the question to Mr. Rose. Mr. Rose said, "Yes, that sales or the receivables were virtually all collected and no delinquencies were being experienced." (Hieronymus Dep., p. 35)

D 302. Rose discussed with Hieronymus a Topper program whereby internal auditors went into the field to check that material was moving off store shelves and a perpetual inventory system to coordinate purchasing and manufacturing and to make sure there were sufficient raw materials available. (Hieronymus Tr., p. 593)

D 303. Rose also discussed a computer program, which Hieronymus thought was very interesting, for checking Topper's accounts receivable and past accounts receivable. (Hieronymus Tr., p. 593)

D 304. During the trip back to New York, Downs told Hieronymus that he had been instrumental in obtaining a secured $7 million long-term credit agreement with Ford Motor Credit which contained provisions whereby, if Topper met certain conditions, it could become an unsecured loan. (Hieronymus Tr., p. 594; PX 1417 at 5)

D305. After his return to his office, Hieronymus prepared PX 1417 on the basis of the Private Placement Memorandum and information gathered on his trip to Topper. (Hieronymus Tr., p. 596; ADM 165)

In his memorandum on his trip, Hieronymus stated that while the reliability of toy manufacturers' forecasts are highly suspect, expected results in Topper's case had an exceptional degree of accuracy. He stated that the reason for this is that Topper had already received $53 million in orders, that total projected sales were $68 million and that the next two months customarily represented the heaviest part of the ordering season. (PX 1417 at 1) Relative to the Dawn line, Hieronymus noted that sales volume had already reached $30 million. (PX 1417 at 2)

D 306. In addition to these factors, Hieronymus also felt that the Sesame Street products would greatly improve the prospects of Topper in the following year. Hieronymus Tr., pp. 596-597)

D 307. On August 17, the date that Hieronymus prepared PX 1417, he got a phone call from Inglis. Inglis mentioned some revisions in the proposed purchase agreement and also said that Hieronymus would be supplied with a break-even analysis of Topper and information as to various examples of Topper's reporting system. Inglis told Hieronymus that the deal was firming up. He said that due to the good response they were having they were going to increase the amount from the originally planned $5 million to $7 million.

Inglis gave Hieronymus names of institutions seriously considering participating, including American National Insurance Company. Hieronymus said that the Pension Fund had indicated that it "had progressed into the later stages of having approved $3 million" and that various other pension funds had "circled" $2 million. (Hieronymus Tr., pp. 597-598; PX 1419; ADM 146)

D308. On or about August 19, 1971, Rose provided Connecticut Mutual with PX 1418, which included, among other things, an analysis of gross margin by product line for 1970 and 1971, which reported that Topper sales of the Dawn line of dolls in 1970 were $34,155,000, or more than half, of the total 1970 sales of $63,936,000. (ADM 147)

D 309. On August 24, 1971, Hieronymus talked with Rosenblatt of Korvette's. Rosenblatt told Hieronymus that 1971 was not a good year for toys. (PX 1422) Hieronymus did not ask Rosenblatt whether Topper was doing any bill and hold in 1971. Similarly, Hieronymus asked Rosenblatt no questions about Topper's return or exchange policies. (Hieronymus Tr., pp. 623-624)

D 310. On or about August 25, 1971, Hieronymus talked with Bailey of W. T. Grant. Hieronymus did not ask Bailey whether Topper was doing any bill and hold in 1971, nor any questions about Topper's policies as to the return or exchange of merchandise. (Hieronymus Tr., pp. 623-624) Bailey was very guarded in his comments about the success of any toy from season to season. He said that due to the tough nature of the industry, a hot item one year, like Dawn dolls, might not sell at all well the next year. Bailey said that Topper did not stand above some other toy companies such as Louis Marx in plastic toys, Milton Bradley in games, and Ideal. (PX 1421)

D 311. Hieronymus did nothing additional relative to the Topper matter prior to Weir's return from vacation on August 30. (Hieronymus Tr., p. 604) After Weir had read Hieronymus' trip memorandum, Weir and Hieronymus talked about the spread sheets on Topper and Topper's products. At that time they had a better idea of what the conversion price might be on the convertible issue and talked about possible rates of return related to the risk involved. Some of the risks they discussed were that Topper had incurred substantial losses, that the coverages of the fixed charges were low by Connecticut Mutual standards, and that Topper relied heavily on bank financing. Weir thought Bates, Connecticut Mutual's President, should be approached. (Hieronymus Tr., pp. 604-605)

D 312. Weir asked Hieronymus to make up an Industrial Summary Sheet which Weir could use in talking with Bates. Weir started on August 30 and spent approximately three days making up the sheet. (PX 1423; Hieronymus Tr., pp. 605-606; ADM 175) Hieronymus gave the Industrial Summary Sheet (PX 1423) to Weir on September 1, 1971. (ADM 176)

D 313. The Industrial Summary Sheet prepared by Hieronymus stated that Topper's intended use of proceeds from the Private Placement was to "reduce secured bank borrowings incurred to carry inventories and accounts receivable" and Connecticut Mutual knew that the proceeds would be so used. (PX 1423 at 1; ADM 186)

D 314. Prior to the Private Placement, Connecticut Mutual concluded that it was reasonable to expect a market price for Topper common stock of $29 in 1973, and that in light of the conversion price provided for in the Private Placement, this would represent a 24% overall return to Connecticut Mutual on its investment in the Private Placement. (PX 1423 at 10; ADM 148) Connecticut Mutual also concluded that there was above average risk in investment in the Private Placement. (PX 1423 at 11; ADM 149)

D 315. During the week of August 30, Hieronymus received several phone calls from Inglis, asking why Connecticut Mutual was taking so long to make up its mind on Topper, and telling Hieronymus that the participants on the Private Placement were firming up, that U.S. Steel would be going ahead for $3 million and that Princeton University Endowment Fund was going ahead for $1 million, based upon the enthusiasm that Molé had for Topper. Inglis said that Molé was directly involved in the negotiations and that Molé had become very optimistic about the outcome. Inglis also said that if Hieronymus had any questions, he should come and visit with Topper again to clear them up. (Hieronymus Tr., pp. 606-608)

D 316. Hieronymus asked Inglis whether the banks were willing to go unsecured. Inglis said he had checked with Topper and found out that the banks were not willing to go unsecured until some time after the year-end figures were available. Inglis said that the banks had been with Topper a long time, had been through a lot of trials with Topper, knew Topper management well and felt comfortable with it. (Hieronymus Tr., pp. 608-609) Inglis also told Hieronymus about Thompson's check with Citibank. If he had not been told this, Hieronymus would have checked with either Citibank or Manufacturers Hanover. (Hieronymus Tr., p. 609; Hieronymus Dep., p. 101)

D 317. Hieronymus did not, during his investigation into Topper, ask anyone about or obtain any knowledge as to what information was being supplied to Citibank by Topper. (Hieronymus Tr., pp. 619-620)

D 318. During Hieronymus' investigation Rose had mentioned to him that Topper had a program whereby an aging of its accounts receivable could be prepared quickly after the end of the month. Hieronymus received and looked at the Examples of Company's Reporting (PX 1459; Hieronymus Tr., p. 621) but did not, however, ask to see any reports which he discussed with Rose or saw therein. (Hieronymus Tr., p. 623)

D 319. Hieronymus was given full access to Topper's records and was free to check anything he wanted to check. (Orenstein Dep., pp. 446-448; Inglis Dep., pp. 88-89; Hieronymus Tr., p. 623)

D 320. Weir read the Industrial Summary Sheet several times prior to meeting with Bates during the afternoon of September 2. (ADM 182) During that meeting Bates read the Industrial Summary Sheet and discussed it with Weir. (ADM 190) The purpose of the meeting was "to review those potential investments that might be placed on the agenda of the meeting of the Executive Committee on September 3, 1971." (CM Ans. to Interrog. (2d Set) 14(c)) The determination that the topic of participation in the Private Placement should be placed on the agenda for the September 3, 1971 Executive Committee meeting "required the concurrence of both Bates and Weir." (CM Ans. to Interrog. (2d Set) 14(f); ADM 187)

D 321. By the end of his meeting with Weir on September 2, 1971, Bates, who had no knowledge of Thompson's check with Citibank, had concluded that participation in the Private Placement should be recommended, subject only to the receipt of no materially adverse information concerning Topper. (CM Ans. to Interrog. (2d Set) 14(e); CM Ans. to Supplementary Questions 22-23, 25)

D 322. Bates reviewed the Industrial Summary Sheet (PX 1423) prepared by Hieronymus on Topper. This sheet says nothing about Citibank and does not refer to Thompson's check with Citibank. The only document concerning Topper that the other members of the Executive Committee saw prior to their authorization of Topper investment was the Executive Committee Memorandum dated September 2, 1971. (PX 1425) This document similarly makes no reference to Citibank or to Thompson's check with Citibank. (ADM 194; PX 1423; PX 1425)

D323. Weir asked Hieronymus to prepare PX 1425, an Executive Committee Memorandum which was presented to the Executive Committee members. This memorandum made no mention of Citibank. The Executive Committee met on the morning of September 3 and authorized management to go ahead with the Topper investment. (Hieronymus Tr., pp. 612-613)

D 324. It was not until after the September 2nd meeting between Weir and Bates that Hieronymus told Weir about Inglis' mention of Thompson's check with the banks. (Hieronymus Tr., pp. 610-611)

D 325. During the week following the Executive Committee's authorization, Inglis notified Hieronymus that American

National Insurance Company and the Princeton University Endowment Fund had dropped out of the Private Placement, and that the deal was cut back to $5,250,000. (Hieronymus Dep., pp. 108-110; ADM 146) Inglis told Hieronymus that someone at American National had overstepped his bounds and that the investment had been turned down at higher levels. Inglis told Hieronymus that there was a misunderstanding between Molé and the person actually running the Princeton Fund, and that the latter did not want to participate. Inglis relayed this information to Weir. (Hieronymus Tr., pp. 613-614)

D 326. Hieronymus did not inquire as to the reason why the Topper investment had been turned down at "higher levels" at American National, nor why the Princeton Fund decided that Topper was not an investment it wanted to make. (Hieronymus Tr., pp. 627-628)

D 327. On January 21, 1972 Hieronymus wrote a memorandum concerning the Private Placement, in which he listed "a chronology of events and facts that led up to" Connecticut Mutual's investment in Topper. Nowhere in such chronology, which covers the period from July 16, 1971 to September 28, 1971, is there any reference to Citibank or to Hieronymus' phone call with Inglis in which Thompson's check with the banks was mentioned. (CBX 15)

VIII. Dallas Bank Investigation

D 328. The Dallas Bank, which had discretionary investment authority as to the Omega Trust's assets (Gray Dep., pp. 10-13), first learned of the Private Placement through a phone call from James Ledbetter of Bernstein-Macaulay to Marvin Jaynes on or about September 16, 1971. Ledbetter explained to Jaynes what it was about and why he thought it was a good investment. (ADM 197-198)

D 329. Subsequent to the phone call, Ledbetter sent Jaynes a copy of the Private Placement Memorandum. This was the only document concerning Topper which Jaynes or anyone else at the Dallas Bank saw prior to the Private Placement. (ADM 199-200)

D 330. After reading the Private Placement Memorandum, Jaynes told Ledbetter that the Dallas Bank did not want to participate in the Private Placement. Shortly thereafter, Ledbetter called Jaynes and asked him if the Dallas Bank would be interested in taking a smaller participation in the Private Placement than Ledbetter had initially suggested. (ADM 201-202)

D 331. John M. Gray, Chairman and Chief Executive Officer of the Dallas Bank, received a telephone call from William Tinsley, a partner of Wynne, Jaffe and Tinsley, which was counsel of the Dallas Bank and Omega-Alpha Inc. (the parent of the Okonite Pool Trust), as well as a director of both the Dallas Bank and Omega-Alpha, Inc. In the course of that call, Tinsley told Gray that he had received a very troubled call from Marshall Cogan to the effect that the Dallas Bank had apparently rejected an investment in Topper debentures which Hayden Stone wanted made on behalf of the Omega-Alpha, Inc. Pool Trust and that Tinsley wanted Gray to look into the matter, and see if there was something the Dallas Bank could do to help them. Gray viewed that call of such sufficient anxiety that Cogan had interrupted Tinsley's luncheon in Atlanta, Georgia to get his message through. Tinsley indicated that the Dallas Bank might lose the trust account if it did not go along with Hayden Stone. Gray told Tinsley that his trust department felt strongly that the Topper debentures should not be purchased but that he would look into the matter. (ADM 203; Gray Dep., pp. 24-27, 38-41, 63; Tinsley Dep., pp. 18-23)

D 332. Subsequently, Jaynes received a call from Gray to inquire why Jaynes had refused to participate in the Private Placement. Jaynes thereafter met with Gray and reviewed the Private Placement Memorandum with him. (ADM 204-205)

D 333. In the course of Gray's meeting with Jaynes, Jaynes presented Gray with the documentation that he had and summarized his analysis of the investment and proceeded to convince Gray that his judgment was correct. Gray's initial reaction was to sustain Marvin Jaynes' decision. Jaynes' decision, according to Gray, focused on the speculative character of the proposed investment and the fact that, in his opinion, it failed to meet the standards of quality of an investment that should go into the pension trust. Upon reviewing the documentation on Topper and discussing it with Jaynes, Gray concluded that the investment should not be made. (ADM 206; Gray Dep., pp. 28-34; Jaynes Dep., pp. 27-28)

D 334. Within a day or two following Tinsley's call to Gray and Gray's meeting with Jaynes, Tinsley returned to Dallas and came to Gray's office and inquired as to what disposition had been made of the Topper matter. Gray and Jaynes outlined to Tinsley why the Dallas Bank had rejected, up to that point, the investment. During that same meeting, but subsequent to that discussion with regard to the merits of the proposed investment, and very likely after Jaynes had left the room, Gray and Tinsley rationalized together and it was summarized that the recommendation had been made by Bernstein-Macaulay, who was designated as the investment counsel for a fee for the Omega-Alpha Trust; that the substantial portion of the debentures was going to be purchased by the U.S. Steel Pension Fund and some insurance company on the East Coast and that the Dallas Bank's part of it, $250,000, relative to the $5,000,000, was not all that consequential; and that it would be an accommodation to Hayden Stone for the Dallas Bank to do it. However, at that meeting Gray concluded that since Hayden Stone or Bernstein-Macaulay was going to be calling the shots in a way that might not meet with the Dallas Bank's approval, the Dallas Bank would be better off abandoning both the authority and the responsibility for making investments in this Fund and would proceed immediately with the mechanics so that the Bank could abdicate investment responsibility and simply be a custodial agent. It was on that basis that Gray agreed with Tinsley that the decision would be reversed and that he would instruct Marvin Jaynes to make the investment. (ADM 207-208; Gray Dep., pp. 35-36; Tinsley Dep., pp. 40-41)

D335. Gray then instructed Jaynes to purchase $250,000 of Topper debentures in the Private Placement. Thereafter, on or about September 27, 1971, Jaynes called Ledbetter and told him that the Dallas Bank would buy $250,000 of Topper debentures in the Private Placement. (ADM 209)

D336. Jaynes considered the Topper Private Placement speculative in nature and an inappropriate investment for the Dallas Bank to make on behalf of the Omega-Alpha, Inc. Pool Trust. (ADM 210)

D337. There was no contact whatsoever between Citibank and the Dallas Bank relative to Topper.

D338. Prior to the Private Placement, the Dallas Bank did not know that Citibank was lending money to Topper. (ADM 195)

D339. Prior to the Private Placement, the Dallas Bank did not know that the Pension Fund had contacted Citibank concerning Topper. (ADM 196)

D 340. Prior to the Private Placement, the Dallas Bank knew that Topper intended to use the proceeds thereof to reduce its bank indebtedness. (PX 462 at 5; ADM 212)

D 341. The Dallas Bank did not rely upon Citibank relative to its investment in Topper.

IX. Local 816 Pension Fund Investigation

D 342. Solomon, Administrator of Local 816 Pension Fund, was first contacted concerning the Private Placement on September 22, 1971 by Bernstein. Bernstein-Macaulay was the investment advisor for Local 816 Pension Fund. After the phone conversation, Bernstein sent Solomon a letter recommending investment in the Private Placement. (PX 1501) Bernstein sent sufficient quantities of the letter to distribute to all of the trustees of Local 816 Pension Fund. (Solomon Tr., pp. 907-909)

D 343. Solomon sent PX 1501 to each of the trustees with a covering letter. (PX 1501A) All of the trustees approved the investment, and Solomon advised Bernstein by telephone on September 24, 1971 of their approval and followed up with a letter to that effect. (Solomon Tr., pp. 910-911; PX 1530)

D 344. The only information which any representative of the Local 816 Pension Fund knew concerning Topper prior to the Private Placement was contained in PX 1501. No representative had any communication with any person other than Peter Bernstein concerning Topper prior to the Private Placement. (Local 816 ADM 213)

D 345. Prior to the Private Placement, the Local 816 Pension Fund had no contact with Citibank relative to Topper, did not know that Citibank had loaned money or was loaning money to Topper, and did not know that any other purchaser in the Private Placement had contacted Citibank concerning Topper. (Solomon Tr., pp. 911-912; Local 816 ADM (Set No. 1) 1-2)

D 346. The Local 816 Pension Fund did not rely upon Citibank in connection with its investment in Topper.

X. Ford Motor Credit Investigation and Loan

D 347. Ralph Pompea was one of the two loan officers in the Commercial, Industrial and Real Estate ("CIR") Department of Ford Motor Credit responsible for developing and negotiating new investments; making a preliminary credit evaluation to determine whether a transaction was feasible; issuing (upon such determination) a letter of intent which "sketched out the transaction in preliminary detail"; submitting (upon acceptance of the letter of intent by the potential borrower) the proposed investment to the Credit Department of Ford Motor Credit for credit evaluation; working (upon completion of a satisfactory credit evaluation) with the Credit Department to develop a proposal and presenting the proposal to the CIR Credit Committee and the Finance Committee for approval; and drafting (upon such approval) a Commitment Letter for approval by the Ford Motor Credit legal staff and the potential borrower. (ADM HS 246)

D 348. The initial contact between Topper and Ford Motor Credit was made by Joseph Arnstein and Allen Peters in late March or early April, 1971. Peters purported to be an investment banker acting on behalf of Topper. Subsequent to the closing of Ford Motor Credit's loan to Topper,Peters was paid a finder's fee by Topper for introducing Ford Motor Credit to Topper. (ADM HS 250; Pompea Dep., p. 14)

D 349. Thereafter, Pompea met with Downs, Executive Vice President - Corporate Development of Topper, on May 7, 1971 to sketch out the structure of a potential loan to Topper. Among the subjects discussed at that meeting were the centralization of management, the terms of payment of Topper and its competitors, Topper's need for "an improved working capital position" through medium-term financing which would be used to pay down short-term debt, the amount of financing desired by Topper, the interest rate, the nature of the collateral available as security, criteria to be met in order for the loan to become unsecured, and business covenants to become operative in the event that the loan was to become unsecured. (ADM HS 252)

D 350. As a result of Pompea's review of a preliminary prospectus dated March 29, 1971 relating to Topper's April 1971 public offering, Topper's 1970 annual report and reports on Topper in Standard and Poor's and Moody's Industrials, Pompea concluded that a loan to Topper structured as discussed with Downs was potentially feasible. At the instruction of Lavery, the manager of the CIR Department, Pompea issued a letter of intent (PX 1243) to make the loan to Topper, which was subsequently accepted by Topper. (ADM HS 253-255; Pompea Dep., pp. 31-33, 54)

D 351. During a visit to Topper's premises in Elizabeth, New Jersey on May 28, 1971 Pompea had discussions with Henry Orenstein, Downs, Jack Rose and the Topper employee in charge of manufacturing concerning Topper's extended dating program, its monitoring of sales at retail, its selling methods, Toy

Fair, the nature of Topper's customers, its new products, including Sesame Street, Henry Orenstein's marketing and creative abilities, and the centralization of Topper's management. (ADM HS 256)

D352. Upon receipt of the executed letter of intent from Topper in early June, 1971, Pompea submitted it to Ford Motor Credit's Department, along with materials including Topper's preliminary March 29, 1971 prospectus, its 1970 annual report, a catalog of toys, and the Topper unaudited monthly financial statements and projections which he had received at that time. In charge of the credit evaluation of Topper was William Duncan, the Senior Manager and Senior Credit Officer of Ford Motor Credit, Walter Finan, the Managing Credit Department Officer, and Dave Ellis, the Credit Analyst. (ADM HS 257-258)

D 353. Ellis prepared a "CIR Financing Proposal" (with Schedules I through III attached) to Members of the Finance Committee dated June 28, 1971 (HSX Ford 4). Pompea and Finan reviewed the June 28, 1971 proposal in its final form prior to presentation to the CIR Credit Committee and the Finance Committee. Duncan and Cornwall also reviewed the June 28, 1971 proposal prior to its submission to the two committees. (ADM HS 259)

D 354. Prior to June 28, 1971 during a trip to New York, Pompea was introduced to People at Manufacturers Hanover Trust Company ("Manufacturers Hanover"), including Donald Baker, a senior vice president at Manufacturers Hanover, who had worked with the commercial lending area at Manufacturers Hanover, responsible for handling its share of the loan to Topper by the Lending Banks. The thrust of the meeting was that Manufacturers Hanover, which was just starting an accounts receivable financing operation, might take on the Topper account as its first secured receivable loan in this new department. Manufacturers Hanover declined to act as lead bank along the lines suggested by Downs. (ADM HS 261; HSX Ford 7 at 3; Pompea Dep., pp. 65-67)

D 355. Between June 18 and June 21, 1971, Pompea called Edward Waldman at Citibank, introduced himself as a representative of Ford Motor Credit and told Waldman that Ford Motor Credit was contemplating making a loan to Topper which would be secured by the same collateral which secured the loan to Topper by the Lending Banks. (ADM HS 262)

D 356. On or about June 19, 1971, Ford Motor Credit received from Topper a copy of its Accounts Receivable Detail Trial Balance of May 31, 1971, a computer run showing, among other things, the amounts of all outstanding accounts receivable for each Topper customer, by invoice number, and the aging of such accounts receivable under columns entitled "Current", "30 Days", "60 Days", "90 Days", and "Other". (ADM 218)

D 357. Pompea presented the June 28, 1971 proposal to the CIR Credit Committee at a meeting of that Committee between June 28 and July 1, 1971. The members of the CIR Credit Committee had been supplied with copies of the June 28, 1971 proposal in advance of the meeting. (ADM HS 263)

D 358. At the time he presented the June 28, 1971 proposal, Pompea was aware that approximately $14 million out of Topper's approximately $64 million in sales booked in 1970 were booked in December under Topper's Spring 1971 Program. The June 28, 1971 proposal stated that Mattel had introduced extended dating terms in 1970. (ADM HS 264, 266)

D 359. The June 28, 1971 proposal stated that the manufacture and sale of toys was highly seasonal and that while Topper had attempted to moderate the seasonal fluctuations, it had enjoyed very little success in that regard. (ADM HS 267-268)

D 360. The June 28, 1971 proposal stated that since the period ended February 4, 1967, Topper sales had increased each year and reported profits had increased each year except 1970. (ADM HS 271)

D 361. Included in the June 28, 1971 proposal were five-year profit and loss projections which, the proposal stated, indicated "the company's expectations for the Sesame Street toys which will be introduced on a large scale in 1972 and appear to be optimistic in view of past performance." (ADM HS 272-273)

D 362. The June 28, 1971 proposal stated in part that Topper's 1970 audited financial statements reflected "a weak current position with working capital of $6 million and a relatively heavy debt position with a debt to capital funds ratio of 2.7." (ADM HS 274)

D 363. The June 28, 1971 proposal stated that Topper was not rated by Dun & Bradstreet, which reported trade slowness of up to 120 days. (ADM HS 275, Schedule II at 6)

D 364. The June 28, 1971 proposal contained the following statement:

> "FMCC has made direct checkings with First National City Bank (FNCB) and Manufacturers Hanover, two of the three banks involved in the Topper loan agreement.... FNCB did indicate some disappointment in earnings, but stated that bad debt experience on the accounts receivable has been very good. In summary, the banks feel the present status of the credit to be sound and voice no concern relative to their ability to come out whole in the event of liquidation." (HSX Ford 4, Schedule II, p. 6)

D 365. The June 28, 1971 proposal set forth Topper's net accounts receivable as follows:

1/31/69	12/31/70	4/30/71	5/31/71
$17,222,000	$30,198,000	$21,580,000	$23,019,000

(ADM HS 276)

D 366. The June 28, 1971 proposal stated that in 1971 $2 million of Topper's accounts receivable were redated. (ADM HS 277)

D 367. The June 28, 1971 proposal contained a chart showing the comparative aging of accounts receivable at April 30, 1971 and May 28, 1971 as follows:

	$(000)			
	4/30/71		5/28/71	
	Amount	Percent	Amount	Percent
Current	$20,765	74.6	$13,721	49.7
30	273	1.0	8,853	32.1
60	49	.3	133	.4
90 and prior	5,440	19.5	4,929	17.9
Other	4,874	17.5	5,246	19.0
Credits	(3,596)	(12.9)	(5,286)	(19.1)
Total	$27,805	100.0%	$27,596	100.0%

(ADM HS 278)

D 368. The June 28, 1971 proposal contained a schedule listing accounts receivable as of April 30, 1971 by month of billing as follows:

	$ (000) Amount	Percent
April	$ 3,471	12.4%
March	3,854	13.9
February	806	2.9
January and prior	18,395	66.2
Other	4,874	17.5
Credits	(3,596)	(12.9)
	$27,805	100.0%

(ADM HS 279)

D 369. The June 28, 1971 proposal stated that of Topper's $27,805,000 in total accounts receivable as of April 30, 1971, $4,874,000 was classified as "other" and that Topper found that approximately 50% of the items in the "other" classification were eventually collected and that credits were issued for the remainder. (ADM HS 280)

D 370. The June 28, 1971 proposal stated that Topper returns in 1970 amounted to $3.6 million compared to $1.6 million in 1969. (ADM HS 281)

D 371. The June 28, 1971 proposal contained a reconciliation of Topper's accounts receivable in its aging as of April 30, 1971 and its financial statements for April, 1971, as follows:

	$(000)	
Accounts Receivable		$27,805
Allowance - Uncollectible Accounts	$ 570	
- Unapplied Deductions	115	
- Discounts-Advertising	2,091	
Accrued Estimated Returns	3,668	5,444
		21,361
Other	218	218
Accounts Receivable - Statement		$21,580

(ADM HS 282)

D 372. The June 28, 1971 proposal stated in part as follows:

> "Topper's accounts receivable appear to be of good quality with Kresge representing approximately 8% of sales volume. Other large customers include J.C. Penney, Montgomery Ward, Vornado, Woolworth and W.T. Grant. At 4/30/71 accounts receivable included \$6.8 million due from AAA1 rated companies and \$2.8 million due from companies with A1 ratings or better. Bad debts charged off in 1970 totaled \$84,760 compared with \$70,244 for 1969. Topper was involved with only one bankruptcy account during the past three years involving an account with a balance receivable of \$140,000 on which it recovered in excess of 50% of the balance due."

(ADM HS 286)

D 373. The June 28, 1971 proposal stated under the heading "Summary" (Schedule III, p. 3) as follows:

> "Although the accounts receivable have a high amount of datings and are subject to extended terms and frequent returns, they appear to be adequate collateral for FMCC's proposed loan and additional support is provided by the inventory, fixed assets and life insurance. CIR believes that the proposed collateral, in combination with Borrower's credit, results in a satisfactory transaction for FMCC."

(ADM HS 287)

D 374. Prior to the approval of the June 28, 1971 proposal by the Finance Committee and the CIR Credit Committee, Ford Motor Credit representatives spent several days reviewing Topper records at Topper's premises in Elizabeth, New Jersey and one day reviewing Topper files at Citibank. (Orenstein Dep., pp. 438, 448; Siegel Tr., pp. 1138-1139; Skaar Tr., p. 1361)

D 375. Siegel gave the Ford representatives who reviewed files at Citibank everything they asked for. (Siegel Tr., pp. 1138-1139)

D 376. The June 28, 1971 proposal was neither approved nor rejected at that meeting because several questions were raised by members of the CIR Credit Committee which could not be answered on the basis of information then available. Those questions related to the quality of the collateral. Pompea and Finan visited Topper and Citibank on July 1, 1971 in order to obtain answers to the questions raised by the CIR Credit Committee. (ADM HS 288-289)

D 377. On the July 1, 1971 visit to Topper, Pompea and Finan had discussions with Rose, Downs, Orenstein and Schwartz concerning among other things, the extended dating and redating sales of Topper and certain of its competitors. Pompea and Finan were reassured by Downs "that in his judgment the receivables would collect as contractually called for". (ADM HS 290)

D 378. During the July 1, 1971 visit to Citibank, Pompea and Finan had discussions with Lusk, Siegel and Waldman. During those discussions

> "The bank indicated that the toy industry was a high risk industry; that by definition Topper receivables had an element of risk higher than what might be normally found in receivables associated with other industries, but that in their judgment, in the Bank's judgment there should be no great concern, that the situation, that the accounts would not pay out as contractually called for."

(ADM HS 292)

D 379. On or about July 8, 1971 Pompea submitted to the members of the CIR Credit Committee a memorandum dated July 7, 1971 dealing with the questions raised by them (with Exhibits A through C attached), (HSX Ford 7), which had been prepared by Ellis and was signed by Pompea and Finan. (ADM HS 293)

D 380. Attached to the July 7, 1971 memorandum was a schedule which showed that Topper's 1969 net sales of $53,723,000 had been reduced by "Discounts" of approximately $6.1 million, "Discounts - Adjustments" of $3,589,000 and "Returns" of $1,571,000, and that Topper's 1970 net sales figure of $64 million had been reduced by "Discounts" of approximately $2.4 million, "Discount - Adjustments" of $9,992,000 and "Returns" of $3,645,000. (ADM HS 295-296)

D 381. The July 7, 1971 memorandum indicated that the average collection period for Topper accounts receivable which were included on Topper's balance sheets as at December 31, 1967, 1968, 1969 and 1970 as well as the estimated collection period for Topper's accounts receivable included on Topper's projected balance sheets as at December 31, 1971, 1972, 1973, 1974 and 1975 were as follows:

12/31/67	12/31/68	12/31/69	12/31/70
62 days	87 days	117 days	174 days

12/31/71(E)	12/31/72(E)	12/31/73(E)	12/31/74(E)	12/31/75(E)
153 days	130 days	130 days	133 days	137 days

(ADM HS 297; Pompea Dep., pp. 112-113)

D 382. The July 7, 1971 memorandum indicated that Topper's sales of Dawn in 1970 amounted to $41,401,000. (ADM HS 298)

D 383. On July 8, 1971 the CIR Credit Committee considered the June 28, 1971 proposal, subject to certain conditions. The members of the CIR Credit Committee who approved the June 28, 1971 proposal were R.S. Olson, Chairman of the Board of Directors of Ford Motor Credit; John C. Dean, President of Ford Motor Credit; John A. Jansma, Executive Vice President, Special Finance Operations of Ford Motor Credit; W.H. Guinn, Vice President-Finance of Ford Motor Credit; and Richard S. Cornwall, Vice President of Ford Motor Credit in charge of the CIR Department. The June 28, 1971 proposal was also concurred in by Bernard L. Lavery, Manager and Senior Investment Officer of the CIR Department; William G. Duncan, the Senior Manager and Senior Credit Officer of Ford Motor Credit; and a member of the legal staff of Ford Motor Credit. (ADM HS 299-300)

D 384. Among other reasons, Ford Motor Credit proposed and ultimately made its $7 million loan to Topper for the reasons as well as the analysis set forth in a June 28, 1971 and July 7, 1971 Ford Motor Credit memorandum (HSX Ford 4, 7; ADM 215)

D 385. Because the proposed loan to Topper involved a transaction exceeding $3 million, under Ford Motor Credit's procedures it was necessary that the proposal be ratified not only by the CIR Credit Committee but also by the Finance Committee of Ford Motor Company, the parent company of Ford Motor Credit, composed of senior members of the management of both Ford Motor Credit and Ford Motor Company. The members of the Finance Committee who approved the Topper loan were Olson, Dean and John Sagan, who was the Vice President - Treasurer of Ford Motor Company. Olson and Dean approved the June 28, 1971 proposal on July 8, 1971; Sagan approved it on July 15, 1971, subject to certain conditions. The conditions to which the approval of the Finance Committee was subject were (1) that a default under the loan to Topper from the Lending Banks would constitute a default under the Ford Motor Credit loan to Topper; (2) that Ford Motor Credit would be given an opportunity to review Topper's financial condition and the terms of its loan agreement with Topper as a condition precedent to Ford Motor Credit's releasing its security under the agreement; and (3) that Ford Motor Credit's $7 million loan to Topper would be reduced to $5 million no later than 3 months after the closing of the loan. In addition, the Ford Motor Credit loan commitment was to be conditioned upon there being no material adverse change in Topper's financial condition between the time of the loan commitment and the closing. (ADM HS 301-302, 302(a))

D386. Subsequent to the approval of the Ford Motor Credit loan to Topper by the Finance Committee on July 15, 1971, a commitment letter dated July 15, 1971 (PX 1245) was prepared by Ford Motor Credit and submitted to Topper, by which Ford

Motor Credit advised Topper that it was committed to make a loan to Topper in an amount and upon the terms and conditions set forth therein. The Board of Directors of Topper approved the commitment letter and authorized the borrowing of $7 million from Ford Motor Credit at its meeting on July 27, 1971. (ADM HS 303-304)

D 387. Subsequent to July 15, 1971 Pompea submitted the letter of intent and the commitment letter to the Ford Motor Credit legal staff for preparation of documentation in connection with the Ford Motor Credit loan to Topper. The legal staff of Ford Motor Credit prepared the initial drafts of the Ford Amendment Agreement, Topper's promissory note payable to Ford Motor Credit for $7 million, and the Participation Agreement between Ford Motor Credit and the Lending Banks entered into at the time that the Ford Amendment Agreement took effect. Topper's counsel at White & Case participated in the drafting of subsequent drafts of the Ford Amendment Agreement. (ADM 307-309)

D 388. The Ford Amendment Agreement was dated as of September 17, 1971 (HSX Ramseur 18). The Ford Motor Credit loan to Topper closed on September 16, 1971; and on September 17, 1971 Ford Motor Credit wired the proceeds of its loan to Topper, $7 million, to Citibank, and the proceeds were used to pay down Topper's loan from the Lending Banks. (ADM HS 311)

D 389. At the specific request made to Topper, for several months prior to the closing of the Ford Motor Credit loan to Topper, Ford Motor Credit received, on a daily or weekly basis, Topper's daily Loan Status Reports which contained an analysis of the eligible and ineligible collateral, the loan balance and the amount of the available collateral or overadvance as of such date. The August 16, 1971 Loan Status Report (HSX Ford 6), which was received contemporaneously by Ford Motor Credit, showed an overadvance of $4,087,474.47. (Pompea Dep., pp. 107, 197-198, 253; HSX Ford 6)

D 390. Prior to the closing of the Ford Motor Credit loan to Topper, Pompea knew that accounts receivable more than 60 days past due were ineligible for advances under the Finance Agreement, and that as of August 31, 1971 Topper's accounts receivable 60 days or more past due totaled $8.2 million. (HSX Ford 10; ADM HS 312; Pompea Dep., p. 260)

D 391. Prior to the closing of the Ford Motor Credit loan to Topper, Pompea knew that goods sold and held in field warehouses by Topper as of August 31, 1971 totaled $4.3 million. (HSX Ford 10; Pompea Dep., p. 260)

D 392. Prior to the closing of the Ford Motor Credit loan to Topper, Pompea knew that as of August 31, 1971 Topper had gross accounts receivable of $35,450,000, of which only $17,650,000, or less than 50 percent, were eligible for advances under the Finance Agreement. (HSX Ford 10; Pompea Dep., p. 260)

D 393. Pompea received Topper's July 31, 1971 financial statements from Rose on or about September 23, 1971. On October 19, 1971, Pompea wrote a memorandum to Cornwall, with copies to Duncan and Lavery, of that date (HSX Ford 16), in which he recommended that given Topper's

> "much improved balance sheet position and steady earnings progress, it is suggested that the financial risk associated with FMCC's $7.0 million investment has decreased since the original date of commitment"

and that therefore Ford Motor Credit reconsider the reduction of its loan from $7 million to $5 million within three months of the closing, as originally provided. Pompea summarized therein a portion of Topper's July 31, 1971 financial statements which he had reviewed. (ADM HS 318)

D 394. On October 27, 1971 Finan sent to Duncan a memorandum (HSX Ford 15) with copies to Pompea and Ellis, containing additional financial information and documents concerning Topper, including a summary of comparative sales and earnings for the eight months ended August 31, 1971, taken from Topper's August, 1971 unaudited financial statements. In that memorandum Finan stated, among other things: "I think the $7 million loan is adequately secured and, therefore, would recommend that we retain the full loan." The memorandum also stated that "It appears unlikely that the company will be able to make its 1971 projections calling for Net Sales of $68 million and Net Profit Before Taxes of $5 million. (ADM HS 319; HSX Ford 15)

D 395. On November 17, 1971 Pompea submitted a proposal (HSX Ford 18) to the Ford Motor Company Financing Committee to, among other things, change the borrowing formula under the Ford Amendment Agreement to permit the Lending Banks to make over-advances up to 20% of eligible accounts receivable. The reason for the change was stated as follows:

> "A new formula was adopted in final negotiations with Topper and the banks and based on calculations at that time it appeared to be within the above 80% of 'eligible' requirements. It has now been determined that loans under the new formula incorporated in our loan documents could exceed the 80% of 'eligible' formula."

(HSX Ford 18 at 2)

D 396. On November 23, 1971 Pompea submitted a proposal (HSX Ford 19) to the CIR Credit Committee and to the Ford Motor Company Financing Committee in which it was recommended, among other things, that the Ford Motor Credit loan to Topper be continued at $7 million rather than reduced to $5 million, as originally provided. (ADM HS 321)

D 397. The November 23, 1971 proposal contained a comparative sales summary for the nine months ended 9/30/70 and 9/31/71 as follows:

	(000's) Nine Months Ended	
	9/30/70	9/30/71
Gross Sales	$40,194	$41,970
Less Returns	$ 2,496	$ 1,177
Discounts	2,912	3,014
Total	$ 5,408	$ 4,191
Net Sales	$34,786	$37,779

(ADM HS 322)

D 398. The November 23, 1971 proposal contained a comparative aging of accounts receivable, according to billing terms, as of April 30, 1971 and September 30, 1971 as follows:

(000's)

	4/30/71		9/30/71	
	Amount	%	Amount	%
Current	$20,765	74.6	$18,595	44.6
30 Days	273	1.0	3,570	8.6
60 Days	49	.3	5,877	14.0
90 Days & Prior	5,440	19.5	9,555	22.8
(a) Other Debits	4,874	17.5	4,147	10.0
(b) Other Credits	(3,596)	(12.9)	(32)	(-)
	$27,805	100.0%	$41,712	100.0%
Less Reserves:				
Returns, allowances & Discounts	5,874		5,148	
Uncollectable Accounts	570		570	
	6,444		5,718	
	21,361		35,994	
Other Receivables	541		190	
Per Balance Sheet	21,903		36,184	

(a) Estimated portion of billings that will result in returns allowances and discounts.

(b) Credits allowed for returns, allowances and discounts.

(ADM HS 323)

D 399. The November 23 proposal contained a summary of eligible accounts receivable as of September 30, 1971 as follows:

	(000's)
Eligible Current Accounts	$21,973
Bill & Hold Accounts	4,895
Redated Accounts	1,936
Accounts Past Due Over 60 Days	7,380
	$36,184

D 400. Maximum borrowing power at 9/30/71 was as follows:

Eligible Current Accounts - 80%	$17,578
Bill & Hold Accounts - Maximum	1,000
Redated Accounts - 50% (Max. $1 million)	968
	$19,546
Loans against at 9/30/71	14,836
Excess Borrowing Power	$ 3,710

(ADM HS 324)

D 401. The November 23, 1971 proposal, which included the November 17, 1971 proposal, was approved by the members of the CIR Credit Committee and the members of the Finance Committee, and was concurred in by Duncan, Cornwall, Jansma and a member of the Ford Motor Credit legal staff. The approval of the members of the CIR Credit Committee and the Finance Committee was given on November 24, 1971. (ADM HS 325)

D 402. On December 14, 1971, Orenstein and Downs visited Ford Motor Credit and had discussions with at least Pompea, Cornwall and Lavery. During this visit Topper "dropped the bombshell" on Ford Motor Credit to the effect that Topper anticipated a significant loss which could be as high as its net worth of over $30 million. Pompea's reaction to receiving this information was "suicidal". (ADM HS 326; Pompea Dep., pp. 143-144)

D 403. During that visit Ford Motor Credit was told that Topper had made a decision to cancel the extended dating program for 1972. (ADM HS 327)

D 404. In January 1972, Skaar of Ford Motor Credit had discussions with Siegel concerning Topper. Siegel told Skaar that Ford and everyone else should have been aware that Topper's bill and hold receivables, which Citibank had declared ineligible when it was not provided with the proper documentation from Topper's customers, might not amount to anything. (PX 1551). Siegel told Skaar, however, that his superiors at Citibank never shared his concern with the warehoused receivables, but thought him somewhat of an alarmist. (Skaar Tr., pp. 1364-1365)

D 405. Siegel reviewed with Skaar the increase in ineligible receivables during the Summer of 1971 (PX 1551 at 4; see ¶¶ 52-53 supra), which was fully known to and documented by Ford Motor Credit when it made its loan to Topper on September 17, 1971. (See ¶¶ 390-392 supra) In his memo, Skaar recorded the sequence of everts in late 1971 as follows:

> "The big problem started in November. Again they were very tight but First National assumed receivables could be collected in season, however, there was simply too much merchandise in the market. . . . At the end of November, Topper realized they were in real trouble." (PX 1551 at 4)

On the basis of his discussions with Siegel, Skaar did not feel that Ford Motor Credit had somehow been "taken" with respect to its loan to Topper in September 1971. (Skaar Tr., pp. 1363-1364)

D 406. Ford Motor Credit's loss on its loan to Topper was "in the Three Million to Four Million Dollar range". (ADM HS 328)

XI. Events Subsequent to Private Placement

D 407. After the Private Placement Citibank continued to make regular advances to Topper until December 17, 1971, when it became aware of Topper's serious financial problems. (Lusk Tr.,p. 1078; Waldman Tr.,p. 1262; CBX 130) Citibank resumed making advances to Topper under a new arrangement in early 1972. (Lusk Tr., p. 1118)

D 408. In addition to the $400,000 it advanced on September 30, 1971, Citibank made advances to Topper during October, 1971 which totalled $7.3 million and advances during November, 1971 which totalled $5,450,000; during the first 17 days of December Citibank's advances to Topper totalled $2,275,000. (CBX 130) From early November, 1971 throughout the remainder of 1971, the Topper loan account was in an "overadvance" status; i.e., the loan balance exceeded eligible collateral. (CBX 161)

D 409. Topper's September 30, 1971 financial statements, supplied the Pension Fund in October, 1971, "showed a soundly financed company with improving earnings" and "further profit gains and an increase in net worth." (PX 1390 at 2; PX 1396A at 1; CBX 34; ADM 102) They were reportedly the best nine months' sales and earnings in Topper's history. (CBX 34; PX 1396A at 1)

D 413. During the fall of 1971 Toy & Hobby World continued to report that certain of Topper's productions, including Dawn, were doing well and various securities analysts continued to be optimistic about Topper's earnings. (Byrnes Dep., p. 114; Botte Dep., pp. 119-120; CBX 77)

D 414. The 1971 Christmas season and, therefore, 1971 in general, was a very bad season for all of the major toy manufacturers. (Pierce Dep., pp. 425, 487-495; Hieronymus Dep., pp. 46-48, 77) Mattel Inc. suffered a net loss from continuing operations (before income taxes) of over $50 million for its fiscal year ending after the 1971 Christmas season, compared to net income of approximately $36 million the year before. (CBX 131; ADM 19; Byrnes AMEX Dep., p. 117)

XII. Lending Banks' Loss

D 415 Lending Banks lost approximately $10.9 million on their loans to Topper under the Finance Agreement. (CBX 129) Citibank's share of that loss exceeded $3 million. (Lusk Tr., pp. 1081-1082)

Dated: December 17, 1976
New York, New York

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MR. BICKS: Your Honor, I pray your leave to put this case on behalf of the plaintiffs in the United States Steel case, and with your permission, assisting me in the presentation of the case is Mr. Dailey, sitting on my left.

I would like, if I may, to begin with a brief opening statement and then this morning proceed with the presentation of documentary evidence.

Your Honor, this case grows out of the purchase by plaintiffs of $4-1/4 million of a total of $5-1/4 million of Topper notes on September 28, 1971, via private placement.

The day next following the Private Placement, that is, on September 29th, 1971, the entire proceeds of the Private Placement went to Citibank to reduce a bridge loan that Citibank advanced to Topper a few weeks before to tide it over the summer until the Private Placement.

Of the $4-1/4 million in notes purchased by the plaintiffs, $3 million were purchased by the United States Steel and Carnegie Pension Fund, which for shorthand in the course of trial we will be referring to as the Pension Fund. $1 million was purchased by Connecticut Mutual Life Insurance Company, and one-quarter million or $250,000 was purchased by the National Bank of Commerce of Dallas.

THE COURT: Who do you represent?

MR. BICKS: All three plaintiffs.

The National Bank of Commerce of Dallas as trustee for the Okonite Pool Trust. For convenient reference we will refer throughout the trial to the National Bank of Commerce in that capacity as trustee simply as the Dallas Bank.

So the Pension Fund bought $3 million, Connecticut Mutual bought $1 million and the Dallas Bank bought $1/4 million or $250,000 for a total of $4-1/4 million.

THE COURT: The Pension Fund is the only one that had a contract with Citibank?

MR. BICKS: That is true.

THE COURT: And they are the only ones that had direct communication with Citibank?

MR. BICKS: They are the only ones who spoke directly to Citibank. How the advice was communicated to Connecticut Mutual--

Without arguing the nature of the agreement at this point, which obviously will be the subject of proof, the agreement will speak for itself as to what obligations it imposed on the bank.

Within 60 days after September 28th, Topper announced that its earnings for 1971 would be quite disappointing; and then 80 days after the Private Placement Topper announced to the world that instead of a pre-tax profit of $5 million for 1971, it would show a loss in the range of

$10 to 15 million.

Topper's announcement was that:

"As a result of our being forced to accept returns from some overstocked customers and exchanges from others attempting to balance inventories, our operations for the year as a whole will result in a very substantial loss. We believe that a major portion of our problems have their origins in last year's sales on extended terms. $14 million of last year's September sales were on extended terms."

In point of fact, Topper's losses went way beyond the $10 or 15 million announced in late December, 1971. 6 The fact, as revealed by its proposed balance sheet of May 31, 1972, was that for the end of '70 through '71 and the first couple months of '72, Topper in fact suffered a loss in the range of $37 million within 80 or 90 days following the Private Placement.

Following such losses, on May 7, 1973, Topper was adjudicated a bankrupt, and at least since that date the notes purchased by plaintiffs in this proceeding have been worthless.

THE COURT: They got nothing out of the bankruptcy?

MR. BICKS: That is right, your Honor.

With Te[illegible]er long since gone from this world, now before this Court, then, are the three plaintiffs, the Pension Fund, Connecticut Mutual and the Dallas Bank, on the one hand, and on the other the defendant Citibank.

In ~~R~~esolving the liabilities between those parties, there are two ultimate issues for this Court's judgment. The first is what, if any, duty did Citibank owe to each of these plaintiffs? ~~a~~And the second is did Citibank's conduct at bar measure up to that duty?

Now, resolving those two ultimate issues, let's put aside some generalities.

THE COURT: Would there be an issue as to whether you justifiabily relied?

MR. BICKS: Yes. That is part of the Citibank's duty to measure up.

THE COURT: Assuming ~~the~~ that Citibank's ~~condut~~ conduct did not measure up, would there be an issue that you were contributorily negligent?

MR. BICKS: I was talking about the ultimate questions of is there a duty and, if there was a duty, was it breached. There are subsidiary issues, I assume, under each of those, but for the purpose of focusing the problem initially at least, I suggest it is helpful to bear those two ultimate issues in mind.

If I may, let's put aside from generalities in dealing at all with those issues. Besides the point of abstractions as to the obligations, if any, creditors may have in the case of the corporation issuing securities to those purchasing the securities, besides the point even of the obligations that a bank advancing money on a secured basis may have to a corporation that issues securities, what counts here is the nature of the duties and obligations Citibank had to these particular plaintiffs in the context of this particular case.

In adducing proof on that score, there are two relations to bear in mind. The proof will portray first the relations between Citibank and the Pension Fund and the extent to which Citibank's conduct toward the Pension Fund was transmitted to Connecticut Mutual and harmed the Dallas Bank.

The second relation or area of conduct that is relevant is Citibank's relation with Topper over the years as a secured lender. What ties the two relations together and gives rise to this case is the private placement where Citibank, the plaintiffs contend, breached its relation of trust to the Pension Fund and, in the process, this led the Pension Fund and Connecticut Mutual, with resulting harm not only to those two plaintiffs but to the Dallas Bank as well. And all this in a context where Citibank reaped the benefit of the proceeds to repay its bridge loan from the Private Placement.

THE COURT: All these plaintiffs have settled with the other defendants?

MR. BICKS: That is right, your Honor. In context, if I may sketch it, in a context where Citibank reaped the benefits of the proceeds from a transaction of which it had been aware at least since February of 1971, 8 months before it took place, which transaction it encouraged Topper to embark upon and at the conclusion of which transaction Citibank's breach of trust and misleading Connecticut Mutual was an indispensable aid.

Let's consider first Citibank's relation with the Pension Fund, and that, your Honor, begins in 1950. To take you back into the history of collective bargaining in this country, in the late 1940s and in early 1950 extensive pension benefits were first introduced on a broad scale into collective bargaining agreements. The pioneer was Philip Murray of the Steel Workers, as you recall.

As a result of that, in early 1950 the United States Steel Corporation began to contemplate means more effectively to manage those ~~uns~~ funds it had set aside to meet the pension obligations to its workers.

As a first step, it consolidated the management of three pension trusts under one management, the Pension Fund, which is before this Court today.

In early 1950 it began to build up the best internal management it could for its Pension Fund to manage those funds which were to be set aside to meet its obligations under the then recently concluded collective bargaining agreements.

Endeavoring this task, however, the corporation realized that no matter how good an internal staff it put together, that staff would have to rely on outside advice. Indeed, the first member of the staff, your Honor, was Mr. Harvey Mole, who remained as president of the Pension Fund through the time of the Private Placement and from whom you will be hearing evidence in the course of this trial.

As I said, recognizing that no matter how competent the internal staff was, the need for outside advice would remain. The corporation, via the Pension Fund, arranged at the time the Pension Fund really started building up its internal staff to secure such outside advice from two banks, the Morgan Bank and Citibank.

Why did it turn to those two banks, your Honor? Both banks had long been lead lenders to United States Steel.

Both banks at the time indeed had a principal officer as a director of United States Steel. And so it was only natural, I suggest, that when they started to build up an internal management capability for their Pension Fund they turned to the banks on whom they long relied in another context.

In November of 1950, a contract was entered into with Citibank whereby the Pension Fund entrusted a portion of its securities to Citibank for safekeeping, obliged itself to pay Citibank a fee and Citibank in turn obliged itself not only to hold the securities but to render investment advice from time to time.

THE COURT: The first contract only required investment advice as to the securities held?

MR.BICKS: We will get to that. The first contract obliged Citibank to render investment advice with regard to government securities and other securities held in a custodian account plus cash held by the Pension Fund for investment, butreally, your Honor, that will be the first document we will be getting to and I will be addressing myself to that immediately following my opening statement, if I may.

Over the years how was that contract provision dealt with? Over the years the Pension Fund management met on a regular basis with Citibank investment officers and economists to receive advice or judgment as to general economic trends, as to particular areas for investment, generally with regard to publicly traded securities. They heard on those occasions as to what activity Citibank was taking in areas where Citibank had investment responsibility under the trust, for example, what industries, what particular companies within those industries Citibank deemed most right for investment.

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Each of those meetings was arranged for by a contact or liaison officer at Citibank who was charged with overall responsibility for contact with or liaison with the Pension Fund. That man during periods relevant to this case was named Walter Jeffers.

In addition to meetings held from time to time, Citibank economists and investment officers discussed public securities. From time to time they considered investments in private placements, that is, investment in securities not generally offered to the public. In those circumstances a pattern of relations developed. The Pension Fund would contact its liaison or contact an officer of the bank, advise him of the company or the area in which they were considering a private placement and ask him to arrange for Citibank to make available to the Pension Fund the best information and judgment Citibank had in its possession with regard to that proposed private placement. So there were two areas of functioning here, the general meetings with economists and investment officers that dealt generally with publicly traded securities set up by the contact officer, in this case Mr. Jeffers.

The second area involved particular advice with regard to private placement. There, too, the contact officer would arrange on behalf of the bank for the Pension Fund to have access in the case of each private placement where the Pension Fund sought advice to the best information and judgment in the possession of the bank with regard to the particular investment under consideration.

That's the general background of the Pension Fund's relation with Citibank.

Now the second relation, Citibank's dealings with Topper. That really began in 1966. From time to time in the course of pretrial proceedings before this trial your Honor has heard of Mr. Orenstein.

Mr. Orenstein emigrated to this country in the '50s, set up a toy business with himself and his uncle Marius. In 1960 he sold that toy business to DeLuxe & Reading which was then a well known conglomerate, and in 1966 he and his uncle Marius bought it back from DeLuxe & Reading .

Citibank came into the picture when it advanced $20 million to the corporation Orenstein set up, Topper, to buy his business back from DeLuxe & Reading. Citibank came into the picture not only itself as a lender of funds to Topper but also as an agent for others that loaned money to Topper.

Citibank advanced funds pursuant to an agreement which we will be referring to throughout this trial as a finance agreement. The Finance Agreement appears complicated but essentially it is simple.

THE COURT: Were all those advances secured?

MR. BICKS: Yes. In essence, Topper pledged substantially all its assets to Citibank as agent under the Finance Agreement. Each day every collection Topper Received ~~recieved~~ from each customer went to Citibank. Citibank would then make advances to Topper in such sum as Citibank felt was warranted by the adequacy of the collateral it had on hand.

The essential asset pledged to Citibank and the primary asset to which Citibank looked for its collateral were the receivables of Topper, and the agreement provided that Citibank would advance funds up to 80 percent of those receivables which it, Citibank, deemed eligible as collateral less such reserves as it, Citibank, deemed appropriate.

So under the terms of that agreement each day all Topper's receipts would go not to Topper but to Citibank, and each day or regularly during the course of each week, at least, Citibank would advance funds to Topper needed for its daily operations.

There are three facets of that relation, that is, Citibank's relation with Topper, that appear relevant to this trial. Those three are the moneys Citibank got for its services as agent and lender; second, the access on a daily basis to the guts of Topper's business via the records that were transmitted each day; and third, the power or control over Topper's affairs, particularly its financial affairs, that Citibank's position under the Finance Agreement gave to it.

Let's look at the first, the money Citibank got. As I indicated, when Orenstein bought his business back in '66 from DeLuxe-Reading, $20 million was advanced under the Finance Agreement. Of that $20 million, $10 million was advanced by Manufacturers Hanover. Though Topper paid a rate of 9.47 percent on the $20 million, Manufacturers Hanover was paid by Citibank at a rate of only 7.65 percent. So that Citibank not only got a 9.47 percent rate but practically 2 percent on Manufacturers Hanover's $10 million.

THE COURT: Was that on secured loans?

MR. BICKS: Yes, everything.

THE COURT: What was that securied ~~up~~ by?

MR. BICKS: The assets they secured from Deluxe-Reading. They got to a point where -- one of the first documents we will be putting in this morning -- by 1968 Citibank was netting an effective yield of 16 percent for its role under this agreement.

By 1971, Citibank ended up with more than 50 percent of the compensation paid by ~~Citibank~~ Topper even though at various times of the year it had no more than 24 or 25 percent of the total advanced.

So that Citibank's role as agent here, with the skimming aspect of the interest from all other lenders, was a particularly lucrative relation for Citibank. Indeed, this Topper arrangement was by far the largest loan that Citibank had in its commercial finance division.

The second facet of the relation, if I may turn to it, that is relevant to this case, the information Citibank received on a daily basis from Topper, that consisted not only of each check from each ~~sutomer~~ customers, but each invoice that went out, a loan status report each day, a remittance report delivered by courier each day with the money, at the end of each month an unaudited financial statement and a voluminous analysis of receivables each day sent by the company.

This information gave Citibank an unparalled insight into the daily ups and downs of Topper's business, the ebb and flow of its dealings with customers.

The third facet of the relation that is relevant here, is the power that Citibank had over Topper's affairs by virtue of the terms of the Finance Agreement. That worked in this way. Under the terms of the Finance Agreement, it was Citibank that determined what receivables were eligible or not. That was a judgment which was Citibank's and Citibank's alone.

However, upon that judgment turned the availability of funds to Topper. So simply by altering that judgment, if you will, Topper could be forced either to go out of business or to go outside Citibank to raise money subordinated ~~suberindated~~ to Citibank's loan, and throughout the year Citibank forced Topper to do just that on several occasions.

Among the first documents I will be calling to your Honor's attention this morning are Citibank's actions in '67 and '68 when Topper needed more funds than Citibank thought it could advance and Citibank insisted as a condition to keeping on advancing funds that Topper go outside and bring in money subordinated to Citibank. And that pattern continued from '67 through the date of the Private Placement.

As a result of Citibank's knowledge of Topper's business, as a result truly of Citibank having its finger on the pulse of Topper's operations each day, Citibank recognized as of late '70 that despite the published figures, and this is the phrasing of Citibank, despite the figures being circulated to the world by Topper, Citibank recognized as of the end of 1970, and that is the language of the Citibank memorandum we will be ~~callling~~ calling to your attention later this ~~monring~~ MORNING, Topper was a company that had to be watched closely. That was a year before the Private Placement. Citibank knew, long before the public knew, that Topper was considering its Spring, 1971 Program, and, your Honor, that is the program of $14 million in sales in the last few days of December, 1970. It was that program and that program alone that turned 1970 from a loss year into a profitable year for Topper. That program, if your Honor ~~wojld~~ would recall, involved shipment on five to eight months extended credit terms, that is, the $14 million in merchandise that was reported as ~~as~~ of the last few days of December 1970, was not due to be paid for by customers until May and August of 1971.

As a result of that postponement in payment, early 1971 was ~~wasa~~ difficult time cashwise for Topper. Thus in January, 1971, Topper and Citibank first discussed a public offering for 1971 in the amount of $3 million.

Four weeks later, by February of 1971, Citibank documents show that Topper and Citibank as not only discussing a public offering of $3 million to take place in April or May but a public offering to be upped ~~uppped~~ to $5 million and a Private Placement to follow the public offering, the Private Placement which is the subject of this litigation.

Now, let me move, if I may --

THE COURT: What is the date of that?

MR. BICKS: September 28, 1971.

The earliest date we can place by documentary evidence Citibank's awareness of that private placement is February 23, 1971, approximately seven months before its effectuation.

Now let me tie, if I may, those two relationships together, Citibank's relation with the plaintiffs and Citibank's relation with Topper via the Private Placement.

Two of the plaintiffs, Connecticut Mutual and the Pension Fund, first heard of the Private Placement in either the last part of July or early August, 1971.

The staffs began investigating and considering whether or not the Pension Fund and Connecticut Mutual should participate in the Private Placement, and if I may call to your Honor's attention two names that will be appearing from time to time in the course of this trial, the man at the Pension Fund who was involved initially in considering the proposed private placement and who did much of the initial investigation was the Pension Fund's investment manager named Henry Thompson. You will be hearing from Mole, who was the president and first employee of the Pension Fund, and Henry Thompson, who was the investment manager of the fund.

He began considering the Private Placement in August of 1971 at about the same time a gentleman named Hieronymus, a name easier to say than to spell, began considering the same thing at Connecticut Mutual, both about early August, 1971.

And the consideration by both really followed parallel paths. Both read a private placement memorandum about the Topper notes, which included in it as an exhibit the April 1971 Public Offering Prospectus. Both went out to Topper's New Jersey facility and questioned management of Topper in the ~~peresence~~ PRESENCE, if you will, of one officer from Hayden Stone. Both addressed questions to the management of Topper.

As mid-August came, within the Pension Fund the Pension Fund's Thompson had visited Topper's management by that time on two occasions, had received materials from Topper's management and in mid-August met with the president of the Pension Fund, Mr. Mole, and reported to him the status of his investigation. He reported what he learned thus far, that Topper had a lending relationship with Citibank, that that lending relationship had gone on since 1966, that in the course of his conversations with Topper, Topper had given him, Mr. Thompson, permission to check with the bank as to their view of Topper's financial condition.

So Thompson talked to the president and said, "What's the procedure we follow? We have this investment advisory relation with Citibank, we have had this relation over the years. How do I go about getting whatever information Citibank has and whatever judgment they can offer before we make up our mind what to do?"

Mole told Thompson to check with Jeffers who was the contact man between Citibank and the Pension Fund. Jeffers at that time was a vice president of the bank in charge of its Metals and Mining Group.

So on August 25, 1971, a Wednesday, Thompson called Jeffers. Thompson told Jeffers that the Pension Fund was considering an investment in a proposed private placement of Topper. Thompson told Jeffers that he had been out and visited with Topper management, that he received materials from them, that Topper management had told him, Thompson, of Topper's relation to Citibank and had given him permission to check with Citibank.

Thompson asked Jeffers to arrange for him to receive whatever information Citibank had in its possession that would be useful to the Pension Fund in evaluating the investment. He didn't ask Jeffers to have a particular person call him, he didn't specify to Jeffers who was to render the advice, who was to provide information, who was to be responsible for the material.

Thompson utilized the regular procedure: he went ~~Went~~ to the Pension Fund contact at the bank and said, "Arrange for me to get whatever you have that will enable us to act as intelligently as we can in evaluating this investment."

In response, on Friday, August 27th, Mr. Waldman called Thompson, and obviously this conversation will be the subject of rather extensive testimony at the trial.

In preparation for that conference with Mr. Waldman, Thompson listed the questions on a yellow pad which he had proposed to put to whoever Mr. Jeffers arranged to supply the information from the bank.

Thompson, in the course of this conversation with Waldman, went down his yellow pad, asked Waldman the questions that he had on his pad with regard to Topper's financial condition in the summer of '71. That's what Thompson was interested in. He wasn't interested in whether Citibank thought it had adquate collateral in the event Topper was to go out of business the next day. He had told Jeffers they were considering an investment in a proposed private placement. He repeated the same thing to Waldman. Thompson's interest was in the financial condition of Topper in August of '71.

Without taking you through the length of that conversation, which will be the subject of testimony, in essence the proof will show that Waldman told Thompson there were no problems at Topper, there were no problems with Topper's financial condition in the summer of '71, and that he anticipated none.

That was Friday, August 27th. That afternoon, Thompson dictated a memorandum of that conversation which was typed by Thompson's secretary on a Monday, August 30th, in essence, stating what I have just said to your Honor.

That favorable advice from Citibank was communicated by Thompson to Mr. Mole. In light of that favorable advice, the Pension Fund proceeded to go ahead with the investment.

At the same time, early on in the week of August 30th, Thompson told ~~Ingliss~~ Inglis of Hayden Stone, the Hayden Stone officer who had been dealing in connection with the Private Placement with both the Pension Fund and Connecticut Mutual, of this favorable report from Citibank, and either early or in the middle of the week beginning August 30, 1971, Inglis~~s~~ told Hieronymus of Connecticut Mutual.

That came up in the course of the conversation as follows: Early on Hieronymus had raised a question. Hieronymus, if you remember, is the name from Connecticut Mutual. Hieronymus raised a question with Inglis~~s~~, after this private placement money comes in: Will the banks consider altering the nature of their lending relation with Topper to go either on an unsecured basis or on an other than demand basis?

Inglis~~s~~ reported back to Hieronymus that the bank would not consider doing so at this time but would consider doing so after the results of '71 were in.

In the course of that report, Inglis~~s~~ went on to say, "However, this does not indicate a lack of confidence on Citibank's part in Topper's present condition or in Topper's management.

"Indeed, Thompson of the Pension Fund has gone over this matter with the bank, has checked with them and they gave him a favorable report."

Had Hieronymus not received a favorable report of Thompson's conversation with Waldman via Inglis~~s~~le, his testimony was and will be that he himself had planned to check with the bank. Had he not received a favorable report either from Thompson or via his own check, had Inglis~~s~~le not told him about it, Connecticut Mutual would not have gone ahead. Had those two lead lenders not proceeded, obviously the Private Placement would have aborted.

As of late August, the seine had been thrown wide. The two big fish that hopefully were to be caught were Connecticut Mutual and U.S. Steel, which were to take 80 percent of the deal.

THE COURT: The two of them together took 80 percent?

MR.BICKS: Yes. They were really the lead lenders here.

Once they were aboard, the net was tightened, the little fish were caught up with the big, the little fish being the Dallas Bank and the Connell lenders.

All the while, on August 27th, when Waldman told Thompson, "There are no problems with Topper's financial condition and we will anticipate none," what will the proof show that Waldman himself knew? What will that proof show?

First, That Topper's past due receivables, those receivables which were not paid for more than 60 days after their due date had jumped 600 percent from the last day of June to the last day of July ; not just doubled; not just tripled; had gone up six times from the last day of June to the last day of July.

Second, what did Waldman know as of August 27th? That as of that date more than 50 percent of the total receivables that Citibank was holding as security were ineligible or sour by Citibank's own records. More than 50 percent of the total were sour.

Third, that for the five months preceding the August 27th conversation, Citibank had shown -- excuse me-- Topper had shown a negative cash flow of $11 million, $11 million more had gone out than had come in from their operation.

This negative cash ~~show~~ flow was accounted for largely by the fact that ~~there~~ their cash collections were $10 million short of what they projected at Citibank. That is the third thing Waldman knew as of August 27th.

The fourth thing is that if you view Topper's operations from the May public offering through the Private Placement, during that five-month period they collected

$18 million from outsiders, from the public offering and the Private Placement and another loan, and only $15 million from their own operations, which gives real question as to what the true nature of Topper's business was at that time. Were they in the business of raising money from outsiders or were they in the business of selling toys?

Finally, reflecting all this, Waldman himself on two occasions within forty days of the August 27th conversation had amended the finance agreement to provide a bridge loan to Topper of $5 million, almost exactly the amount of this Private Placement, to tide them over until the Private Placement.

THE COURT: As an unsecured loan?

MR. BICKS: No, in theory secured. It was under the Finance Agreement, but it was a bridge loan, and the Citibank documents so described it and their admissions make clear it was a bridge loan to expire two days after the Private Placement that was due September 30th. The Private Placement closed September 28th. All this Waldman knew on August 27th, when he told Thompson "no problems" with Respect to Topper's financial condition.

THE COURT: I don't know if it is relevant but it is interesting. As a practical matter, could Citibank have gotten out free at that point if it wanted to?

MR.BICKS: It is an interesting speculation.

THE COURT: Do you know one way or another?

MR. BICKS: I don't know. The fact is, less than 60 days later the truth did begin to come out. So what we have here is not a case like Affiliated ~~Youth~~ Ute where the bank stood there mute and didn't say anything and let it all happen. That is not this case, nor is this a case where ~~when~~ Thompson called Jeffers and ~~said to~~ was told by him, either then or later, "I'm sorry, we can't render advice to you here because under the circumstances it is not appropriate."

That would be an interesting case. We don't have either of those. The bank didn't stand mute, because Thompson called and asked for their judgment and advice, and not only did they not stand mute, once Thompson called, they didn't say, "I'm sorry, under these circumstances it is not appropriate for us to communicate information to you or for you to rely on what we say, we have an interest ~~interes~~ in the transaction."

They didn't do either of those. Waldman said, "No problems, and I anticipate no problems with Topper's financial condition," and sixty ~~six~~ days later after the Private Placement the company was under.

That is the essential proof, your Honor.

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MR. WOLLEN: I am not going to take too much time. I do want o make a few remarks and explain in more detail some of the comments that Mr. Bicks went into as to facts that will be shown at the trial.

Briefly, Citibank is charged with a direct violation of Section 10(b), aiding and abetting Topper itself and Mr. Orenstein in violating Section 10(b), and also Section 17 of the 1933 Act, and then being responsible for Topper's violation of both of those statutes on a control basis.

Your Honor was quite right in your questions before to Mr. Bicks. Only U.S. Steel had contact with First National City Bank, and that was a 10-minute telephone conversation that Mr. Bicks has referred to. The Connecticut Mutual plaintiff had no contact whatsoever.

The testimony I think will be in some dispute as to whether Connecticut Mutual even heard about First National City Bank's role prior to the time when it made its decision, but, in any event, it had no contact with First National City Bank, and as has just come out, neither the Dallas Bank nor the Connell plaintiffs purport to have had any contact at all.

Our position, very briefly, your Honor, is that under all these circumstances Citibank did not have a duty of disclosure to anybody, not even United States Steel; that if we did have such a duty, we fulfilled that duty, that we did not make any knowingly false or reckless misstatements of fact, that we had no knowledge of any

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violations by any other parties such as Topper or Mr. Orenstein, and certainly gave no substantial assistance to those parties; and under the circumstances we certainly did not assert any control in the way that term is used in the securities laws over the affairs of Topper, much less this particular transaction.

Your Honor is right also in your question that when First National City started loaning money to Topper in 1966 it was on a fully secured basis. It was secured by accounts receivable. It was not just secured by eligible accounts receivable. It was secured by all accounts receivable, by all inventory, by all machinery, by all equipment. It was secured, in short, by every lock, stock and barrel that Topper owned.

This was not a factoring relationship. As I understand the difference, a factoring relation is where a lender actually makes collections from customers of the borrower. The bank did not do that in this case. Receipts from customers went directly to Topper and, as Mr. Bicks said, the checks would then be turned over to Citibank, and Citibank would apply the receipts against the outstanding balance of the loan.

THE COURT: Topper would just send them to Citibank for deposit?

MR. WOLLEN: That is correct. Topper would receive the checks from customers and would have direct contacts with those customers and turn the checks over to Citibank. The bank did not go around customer to customer and make those collections.

THE COURT: Isn't that what used to be called a non-notice factoring account?

MR. WOLLEN: I have problems with the securities laws. I think it might have been.

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THE COURT: It doesn't make much difference.

MR. WOLLEN: The only point I was making is that the bank was not in direct contact with all these customers. The bank was receiving checks from Topper itself.

In the early years of the loan, the bank would advance funds up to 80 percent of the receivables that the bank deemed to be eligible, plus additional amounts predicated as to stated values for other of Topper's assets. For example, if the bank deemed that Topper's inventory was $2 million, it would advance $2 million specifically against that inventory. If it deemed the machinery and equipment to be worth $1 million, it would advance $1 million against that equipment.

It didn't affect the fact that all of the assets were pledged as collateral for the loan. It just was a method by which you built up the total amount of the outstanding loan that was given.

In later years of the arrangement, and particularly in 1971, the bank did not have what it called -- sub-limits for machinery and equipment and inventory. The bank simply loaned 80 percent of eligible receivables. Occasionally the bank would go above the 80 percent.

THE COURT: Did it have a lien?

MR. WOLLEN:At all times it had a lien on all assets. It did not make specific advances against the receivables or inventory and continued to make advances against 80 percent of receivables,still having a lien on the machinery and inventory against which there were no advances specifically committed at the time. This is in 1971.

In listening to the plaintiffs' opening statement, I came close to confusing Topper with International Business Machine or U.S. Steel itself. This was not a blue chip company, your Honor. If the fact that all of its assets were pledged for its loans it not sufficient, its financial history is clearly sufficient to point that out. It had a checkered financial history. Some years it had big losses and some years it had rather modest profit. It was up and down. The only thing that one could say about its history, as the plaintiffs themselves described in an internal memorandum of theirs, it was turbulent. I think that is a very accurate statement.

The specific charges of the plaintiffs against Citibank ~~City Bank~~ basically are, I think, twofold. I believe it to be twofold. I am not entirely clear about the first aspect of it.

You have heard reference to the fact that Topper instituted a program toward the end of 1971 pursuant to which -- excuse me -- the end of 1970 pursuant to which customers did not have to pay for goods for either five or eight months.

The plaintiffs have contended that it was this program which included the granting to certain customers of return or exchange rights which ultimately caused Topper its problems when those customers declined to pay for the goods and, in fact, attempted to return them to Topper.

The complaint charges that Citibank had actual knoweldge of these practices of Topper, mainly, granting of return rights and exchange rights. The plaintiffs' pretrial brief and opening statement do ~~does~~ not seem to ascribe to the bank~~'s~~ specific knowledge of these privileges that Topper supposedly granted its customers, and I don't believe that there will be any evidence that the bank had any such knowledge. There will be evidence to the effect that certain people at Topper did grant certain customers these rights and that this did contribute in large part to Topper's ultimate problem.

There also will be evidence that people even in Topper and certainly people outside of Topper first learned ~~ot~~ of these rights long after the Private Placement in September of 1971, and, in fact, that this information really did not come to light until January of 1972.

So I don't think there will be any attempt to show that the bank was aware of the underlying business practices that gave rise to Topper's ultimate financial problem.

Also, of course, as a practical matter, those practices would have impacted most adversely upon First National City Bank which had as its collateral receivables and other assets, and it was specifically lending against those receivables. So certainly if the bank had any knowledge of those practices, it would not have continued to advance funds as it did.

What will the bank be charged with knowing? I think it boils down to this, your Honor. That as a result of these alleged practices, there came a time some time in May through the time of the Private Placement in September that the financial information that Topper would generate and that the bank was receiving gave the bank knowledge that Topper was, as the plaintiffs' trial memorandum says, in dire financial condition and about to go bankrupt.

This again arose out of its program that Topper engaged in in late 1970 called the Spring Program. Of course, that program, as Mr. Bicks described it, was disclosed in Topper's annual report for the year 1970 and was disclosed in connection with the public offering that Topper sold in April of 1971. It was a footnote to the financials which disclosed the sale of these goods on extended date and terms. So the program itself was known to all, at least knowable to all.

In May of 1971, it came to the attention of the bank that certain of the receivables that were supposed to have been paid in that month under the 5-month aspect of the Spring Program, 8 months receivables not being payable until the month of August, were not being paid immediately when due.

T1/10 am Mr. Bicks referred to the great increase in past due receivables at the end of July. That is because under the Finance Agreement receivables became ineligible 60 days after the time when they were due if unpaid at that time. So it's in May when these receivables were due, not at the end of July. That's when they became ineligible under the Finance Agreement.

In May, the bank was aware that the receivables were not being fully paid as they were supposed to be, and the matter was discussed with Topper officials throughout May and June and into July.

The Topper officials, and there is clear evidence, continually assured the bank that those receivables would in fact be paid, that they were good receivables, that they would be collected, that in fact the economy was somewhat sour at that time and there were some problems in making retail sales at that time but these were good receivables, they would be paid.

In fact, the Topper officials went so far as to say, "If you insist, we can go out and collect them today. We can make those collections right away, but this would be at the great expense of customer good will and we would much prefer to let them pay them off in due course, but be assured that they will be paid."

So the bank was not alerted that these were a dreadful problem at that point in time. They expected fully that the receivables would be paid and that certainly is evidenced by the fact that we continued to loan money against them.

In fact, there is other evidence to show that the bank was reasonable in believing the statement made to it at that time by Topper officials.

Basically, up to May of 1971 Topper was ~~head~~ ahead of projections in most of its contracts. It was way ahead in its sales. It was certainly not far behind, if at all behind, in its collections.

So up until that point in the year Topper was not doing badly at all. The bank certainly under those circumstances was reasonable in believing that these receivables would be paid in due course.

Topper had just entered into an arrangement which would permit it to come out with a so-~~clled~~ called Sesame Street line which everybody thought was going to be a very strong item in the marketplace and would give Topper such power that it would have no problems at all in increasing its sales and making these collections.

Finally, of course, here the bank was loaning 80 per cent of these receivables but at this point in time we were loaning nothing against the machinery, nothing against inventory, nothing against equipment, yet we had all of that still pledged as collateral. The loan was substantially over-collateralized in the May-June-September period of 1971. This adds to the reasonableness of the bank in accepting the assurances it received from Topper officials.

In July, Topper came to the bank and said, "Because of our increased sales volume which entails increased sales expenses, we need a temporary over-advance."

Prior to that time Topper had informed the bank about its proposed private placement. It did not come to the bank and get the bank's direction as to how to go about the private placement. It told the bank it was going to have a private placement. The bank knew that.

In addition to the Private Placement, Topper had told the bank it was going to secure a rather large amount of money from the Ford Credit Company, Ford Motor Credit Company. The bank knew that also. In the light of those circumstances and the fact the bank did know moneys would be coming into Topper in the fall, in the light of the financial circumstances, the bank officials certainly believed that Topper was in a beter condition at this time than it ever had been in the past. It of course decided to go forward and over-advance funds beyond the 80 percent eligibility expressed in the formula.

Consistently throughout the history of Topper the bank had gone over the 80 percent advance formula on eligible receivables. There was nothing startling, it was nothing that hadn't happened before.

In light of the circumstances at that time, the bank officials believing that Topper was in pretty good financial condition, it was reasonable to do. The plaintiffs in the trial briefs say, and Mr. Bicks in his opening implied, that the advance,over-advance, made in July of 1971 was to keep Topper afloat, just to get the moneys from the plaintiffs in so that the bank could get those moneys right back.

The bank is over-advancing the money to keep Topper afloat for a few months to get the money back from the plaintiffs. I myself don't understand why we would do that, why we would go forward to give money to let Topper perpetrate a fraud so we can get the money right back. It makes no sense to me.

In addition, the bank's actions throughout the summer of 1971 were totally inconsistent with any thought in our mind that Topper was immediately going into bankrupty right after we managed to get these plaintiffs in through the Private Placement.

I mentioned before that Ford Motor Credit

Company had been considering a loan to Topper throughout the summer of 1971. In June and July, Ford Motor officials came to the east and talked to Topper officials, secured information from Topper, came to the bank, sat down and looked at records in the bank and talked to bank officials, and ultimately, in September, 11 days prior to the time of the Private Placement, Ford loaned $7 million to Topper.

Now, Ford did it on a secured basis. They came in on an equal basis with the lending banks. The Ford $7 million was used to reduce the ~~leve~~ level of the other lenders' outstanding balances.

The testimony will be perfectly clear that Citibank was "not happy" with Ford coming in. This was the first instance in which the bank's collateral was being adversely affected, namely, reduced, and, of course, correspondingly the bank's advances were being reduced. But Citibank did not like another bank or another lender coming into that part of the arrangement. That, your Honor, is inconsistent with any thought on the part of the bank that Topper was immediately going bankrupt.

Secondly, in September of 1971, Citibank in effect threw out of the lending group one of the small participants. It stated there wasn't enough income to go around and it didn't want this smaller lender in the group.

There is absolutely no reason if Citibank thought at that time that Topper was going to be in financial condition why it would be letting people get away from the party while inviting the plaintiffs in to share in our losses. It's totally inconsistent with any thought on the part of the bank that Topper was in trouble.

Finally, your Honor, you asked a question before as to whether if the bank really knew in August that Topper was in very grave difficulties, whether Citibank could have gotten all its money back right then.

I don't know the answer to that question. I do know that this was a demand loan, and Citibank could have instanteously gone out and attempted to make all of these connections. I don't know if they would have been able to do so at that time or not, but they could have tried to. They certainly didn't. They continued advancing funds to Topper right on through the time of the Private Placement, right on through the end of the year, long after the Private Placement.

Now let's turn for a minute to the plaintiffs in this case.

The U.S. Steel people had been solicited to invest in Topper previous~~ly~~ to this Private Placement and had declined. On this solicitation, which was made by

Hayden Stone, I think they conducted what might be described as a lengthy investigation. I think the testimony has been and will be that the U.S. Steel people put in over 80 hours at least in their investigation of Topper. They did have meetings with Topper people, they did go out to New Jersey and look at Topper's facility, they did talk to Hayden Stone. They received a lot of documents. There was a private placement memorandum which was prepared by Hayden Stone to Topper and given to the plaintiffs, which they carefully reviewed. They received other documents.

Citibank had no role in that private placement. Citibank did not see the Private Placement Memorandum. Citibank did not see any of the documents that were given to the plaintiff. No Citibank representative went to any of those meetings that were held out at Topper in which the plaintiffs were investigating Topper. In short, Citibank had absolutely no idea of what information had been conveyed by Topper or by Hayden Stone or by anybody else to the plaintiffs in this case. Citibank had no role in that whatsoever. We didn't prepare any papers, we didn't deliver any papers, we had no knowledge of what was in the papers that they did receive.

In short, we just had no idea what the plaintiffs knew.

With that background, then, Mr. Thompson from U.S. Steel calls Mr. Jeffers of Citibank and says that he is considering an investment in Topper. He also said, when Mr. Jeffers expressed some lack of knowledge about what Topper was, he said that it's in the secured part of the bank.

Mr. Jeffers obviously went to the secured part of the bank and he got Mr. Waldman, who is the head of the Factoring and Commercial Financing Department of the bank in which Topper was administered, to call U.S. Steel back.

Mr. Thompson, when he called Mr. Jeffers, did not ask for Citibank's judgment. I don't think he ever said that. What he asked for was information, and he asked for information coming from the secured part of the bank. That's what he got. Mr. Jeffers asked Mr. Waldman from that part of the bank to call Mr. Thompson.

Mr. Waldman did call Mr. Thompson two days later. I don't think there is going to be any great material dispute as to what was said during that conversation. There will be shadings of differences.

As Mr. Bicks pointed out, we are fortunate in this case, in this instance, as we are in a lot of other instances in this case, to have a contemporaneous gwbr

memorandum of the conversation. I think that contemporaneous memorandum does not comport with either what Mr. Thompson testified during the pretrial in this case or the way Mr. Bicks described the conversation, but those pieces will come togehter.

In any event, one thing is perfectly clear and nobody disputes this, it is right in Mr. Thompson's memo. At the end of the conversation Mr. Thompson said to Mr. Waldman, "Well, we're a big pension fund. We don't pay taxes so if we have losses it'sour loss 100 percent. Is this a good investment for us?"

Mr. Waldman says, "I am a credit man. I am not an investment man. I can'tgive you any advice on that."

/12 am And thatwas that. Under those circumstances and considering who Mr. Waldman was and considering who Mr. Thompson was in the investigation that he made, it is our contention Mr. Waldman spoke perfectly honestly. He spoke exactly the way he felt at that time from his standpoint.

No. 2, Mr. Thompson could not possibly have been relying upon Mr. Waldman to tell him that there were absolutely no problems in Topper's financial condition. That just to my mind is incredible.

In any event, as your Honor asked, certainly reliance is a necessary element of the plaintiffs' case. Whatever doubt there is in a class action involving open market transactions, I don't think there is any doubt at all in a private transaction between two parties that reliance is necessary.

It's our contention no reasonable person in Mr. Thompson's position could have relied on what Mr. Waldman told him in the fashion plaintiffs now contend.

The other aspect of the case, your Honor, is the control aspect. The bank is charged with controlling Topper and therefore being responsible for whatever Topper did. Well, the plaintiffs point only to the loans and finance agreement to support their contention that we did control Topper. There is no question that the bank decided how much money to loan Topper and what to take as collateral.

The cases I think are perfectly clear that that is not enough to constitute control. If that were, in any case where a bank is loaning money and has the usual negative powers it would be a control situation. I think the evidence will not be in dispute about that. I think that issue will come out rather clearly, particularly in view of the fact that with respect to the sale of these securities to these plaintiffs Citibank did not control that, did not initiate it and certainly is not subject to that liability.

The custodian agreement. Mr. Bicks is correct, the custodian agreement was entered into in 1950. It provides for the handling of the enormous U.S. Steel account. I think the account is somewhere in the area of $1 billion. The bank performs services under that agreement. It transfers securities. It makes collections, it makes payments, I think it clips coupons. It does all the normal things a custodian does.

The agreement says what their duties are in that respect, and it has one paragraph which says the bank will render investment advice from time to time with reference to securities in the account and cash. That is the paragraph upon which the plaintiffs base that aspect of the case.

Mr. Bicks is also right that from time to time people from U.S. Steel met with people from First National City and talked about the economy. They talked about what types of securities the bank was recommending at the time. They talked about the big picture of the securities world.

Mr. Bicks is also correct that from time to time people from U.S. Steel, mostly going back into the '50s, possibly also the early '60s, would call up and ask for information about some customer of the bank, possibly, or some entity with which the bank had some relationship or some specific knowledge.

In none of those circumstances will it be shown it was investment advice the bank was rendering. The record is perfectly clear this is what Mr. Thompson did when he called Mr. Jeffers on August 25, 1971, and this is what Mr. Waldman did when he called back on August 27th. We are lucky to have memoranda. We also have testimony from U.S. Steel people in pretrial discovery, and all of them refer to the fact that U.S. Steel had a normal policy of conducting a credit check before they went into any investment and that this is what was done. When Mr. Thompson called Mr. Jeffers, he was conducting the credit check. Where do you go to conduct a credit check? The U.S. Steel people testified you go to the lead bank. That is what was done here. The testimony indeed is if the lead bank in this situation had been Chase Manhattan, had been any other bank, they would have gone to that bank in exactly the same fashion as as they went to First National City.

If in fact the plaintiffs in this case, particularly U.S. Steel, had asked for investment advice about Topper from Citibank, they wouldn't have gotten any because Citibank had ~~not~~ no information about Topper in its advisory department. The only place where any information about Topper was was in the Factoring and Commercial Financing Department, from which Citibank's investment people at that time were precluded. They could not go and have access to those files. I think the record will show that this was a credit check conducted by U.S. Steel and nothing else, and obviously that is borne out by Mr. Waldman's specific declining to make a recommendation or give advice at the end of his telephone conversation with Mr. Thompson.

In short, your Honor, we have a lot of records in this case. You will be given a lot of documents, I am afraid. You will receive a lot of depositions and you will hear some testimony. I really think we are fortunate in having so many contemporaneous records and memoranda, and I would urge your Honor to focus specifically on the documents tha were created at the time when the events were going forward.

For example, in the entire Connecticut Mutual file there are a lot of memoranda about the investigation, a lot of memoranda about checking out the investment. There is a memorandum to their investment committee which made the decision to make the investment. There is not one single mention of Citibank, there is not one mention at all.

It is these contemporaneous memoranda that will show what the facts were back in 1971.

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MP 1

AFTERNOON SESSION

2:25 p.m.

THE COURT: You may proceed.

MR. DAILEY: Your Honor, at this time the plaintiffs would like to call Ira Weiss to testify as an expert witness.

IRA CARL WEISS, called as a witness by the plaintiffs, being first duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. DAILEY:

Q Mr. Weiss, will you state your present occupation, please.

A Yes. I am a manager with Price, Waterhouse & Company.

THE COURT: You are a manager?

THE WITNESS: Yes.

THE COURT: What does that mean?

THE WITNESS: There are four levels of staff at Price, Waterhouse & Company. The top level is the partner level; the second level would be the manager level; the third level is the senior level, and the fourth level would be the staff accountant level.

Q Are you a Certified Public Accountant?

A Yes.

Q When were you certified?

A 1970.

Q Is Price, Waterhouse a national accounting firm?

THE COURT: Yes.

A Well, actually, it's an international accounting firm.

Q When did you begin with Price Waterhouse, Mr. Weiss?

A I began with Price Waterhouse IN June 1966.

Q And prior to that, what were you doing?

A Prior to that, I was a student at City College of New York.

Q And what degree did you receive at City College?

A B. B. A.

Q Would you describe for us your initial responsibilities at Price Waterhouse when you started, in 1966?

A Well, when I started with Price, Waterhouse, in 1966, I was a staff accountant. The normal responsibilities of a staff accountant is to audit individual areas within the financial statement. For example, as you might know, the financial statements are broken down into cash, accounts receivable, payables, et cetera, et cetera. As a staff accountant, one is responsible for auditing, let's say, just cash and coming up with the conclusion as to the fairness of cash.

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Q Before we go into particular details, could you tell us approximately in how many audits you have participated as a staff accoauntant?

A Oh, one to two dozen. It's sort of hard to say. About two dozen.

Q And these audits took place during what time?

A Well, starting in July 1966, I had a brief stint with the Army and ending when I got promoted to senior, July 1970.

THE COURT: When did you become a C.P.A.?

THE WITNESS: I became a C.P.A. in March 1970.

Q And in how many audits have you participated in your capacity as a senior?

A About a dozen.

Q And how many in your capacity as a manager?

A About half a dozen.

Q So you have been involved in approximately thirty audits?

A Yes.

Q For Price, Waterhouse?

A Yes.

Q Going back to your initial functions as a staff accountant, would you describe for us what experience, if any, you had in the area of auditing accounts receivable for companies?

A Well, as a staff accountant I was primarily responsible for auditing accounts receivable in a number of audits, and basically that audit would consist of two phases. The first phase would be the gathering of outside evidence to assure ourselves that the accounts receivable were fairly stated, outside evidence considered the best evidence received.

Secondarily, we basically rely on internal reports issued by the company. These internal reports ranged from sales orders, shipping documents, accounts receivable ageings and things like that.

Q Would you explain to us what an account receivable ageing is?

A An accounts receivable ageing would be a listing by customer, and generally you would have the customer named, the total balance due from that customer, and then, depending upon the type of industry, it would be aged.

Normally, I guess you'd see a zero to thirty days would be considered current; thirty-one to sixty days would be considered overdue; beyond that you would have problems, and you would basically be analyzing those problems.

Q When you say zero to thirty and thirty-one to sixty, what do you mean?

A That's days.

Q What is the point of reference?

A Well, the point of reference really depends upon the client itself. For example, in the shipping industry, an account receivable is considered overdue if it's seven days old.

Q And by seven days old, you mean from the due date on he invoice?

A That's right. From the bill of lading date.

Q Is there any significance attached generally to the age of accounts receivable?

A Oh, yes. Very much so. Generally, the older the receivable, the less probability there is of collecting it. Generally, if you have a very old receivable, you have to wonder as to why it's so old. Generally, there's a disagreement between the customer and the manufacturer, and that usually is investigated as part of the audit.

Q Did all the clients for whom you performed services at Price, Waterhouse maintain a system of accounts receivable?

A Yes; they all maintained a system of accounts receivable, for the most part, but --

THE COURT: They all maintained it for the most part, but what?

THE WITNESS: Well, there are some clients that I had that didn't have any accounts receivable to speak of: retail clients in particular, especially retail clients that would serve the mass, sort of like discount stores, where they would rely on BankAmericard and Master Charge. Now, for the most part, BankAmericard and Master Charge are cash, because basically those two particular cards in most cases would render cash to the retailer at the end of the day.

So that, for example, you might have at the end of a year $25,000,000 in sales and $320,000 in receivables. Receivables were relatively negligible to the overall well-being of the company.

Q During the course of your years at the Price, Waterhouse & Company, did you have occasion to review any cash flow projections?

A Oh, yes. Cash flow projections are considered an extremely important aspect of the audit. Basically, it is, for example -- you can have a profitable company, and yet that company, in the next year or the year after, might have an extremely difficult time of making it. The reason why, to give you an example:

Let's just say that you are in an industry where you have heavy capitalization, and you borrow the money for the heavy capitalization, and that money is due, let's say, within the next year; a significant amount is due. You might have a profitable situation, but the cash flow would be just impossible.

So that's why cash flow is an extremely important aspect of our audit and subject to review.

MR. WOLLEN: Your Honor, I think the witness ~~hould~~ should be instructed to answer responsively. It is very hard for me to keep up --

THE COURT: That is a proper observation.

Q Would you explain the purpose for which Price, Waterhouse during the course of its audit reviewed the cash flow projections?

A Well, again, in order to be sure that we had a going-concern basis.

Q Do you know whether as a matter of practice during the years subsequent to the audit, the clients, the businesses themselves, matched actual performance during the year with the projected performance on the cash flow projections?

A Well, not all the companies are the same, but as a standard basis, normally they had them on a month-by-month basis, a matching of actual expenses versus budgeted and an analysis of the variations or the differences.

Q And were these done during any period of time?

A Monthly, usually, for many of my clients.

Q Would you describe and tell us briefly the range of business which the clients of Price, Waterhouse which you audited were engaged?

A Well, they really ranged all over the map. They were basically shipping companies, manufacturing concerns, and I had a couple of retail operations, one of ~~whic h~~ which was a food -- food retailer and the other one was a toy retailer.

THE COURT: What the other one?

THE WITNESS: A toy retailer, the other one.

Q Are you free to tell us the identity of the toy retailer?

A Yes; it was Lionel-Leisure.

Q Lionel-Leisure?

A Yes.

Q Where was Lionel located?

A Lionel is located in Philadelphia.

Q What aspects of the toy business was Lionel engaged in?

A Lionel was a toy retailer. One of their subsidiaries was a toy retailer.

Q Did they distribute at all to other retailers?

A On occasions they might, but it wasn't a significant part of their business.

Q Did they manufacture at all?

A No.

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THE COURT: Aren't they in trains?

THE WITNESS: Well, they were the train people at one time. They sold that operation to General Mills.

Q From what manufacturers did Lionel purchase?

A Well, all the major ones. You had Hasbrough, Ideal, Topper, Matell, Kenney, Milton Bradley.

Q What was the time frame youwere working on the Lionel audit?

A I was the senior in charge of the exam on the December 31, 1970 audit and the December 1971 audit.

Q As a senior, what were your responsibilities?

A I was overall responsible for the field work. In other words, what I did was, I supervised the assistants doing the work, and I reviewed all their files.

THE COURT: May I ask, is this just to qualify him as an expert, or are you going to have substantive testimony regarding this?

MR. DAILEY: The purpose is to qualify him not only as an expert but as an accountant eminently qualified in the toy industry.

THE COURT: You mentioned Topper. Is there going to be substantive testimony about Topper?

MR. DAILEY: To some extent, your Honor, and the evidence is offered to establish Mr. Weiss' credentials as an accountant familiar with the toy industry.

When we get to the financial information, I think he can ~~shet~~ shed more light on the state of his knowledge of the industry.

Q The first audit you worked on with Lionel was for the fiscal year ending December 31, 1970?

A That's correct.

Q When did you commence your responsibilities in connection with that audit?

A Well, I was assigned to the audit around September of 1970.

Q When was the first time during the course of this audit, if at all, that you heard of Topper Corporation?

A In September of 1970.

Q And in what connection did Topper come to your attention?

A Well, as a normal course -- in the normal course of our work, ~~wha~~ what I would do is sit down with my predecessor senior and the staff that worked on the job to find out significant problems ~~tha t~~ that they might have, and one of the problems that they were concerned with was the problem of inventory, and specifically a very large problem was the particular toy called Johnny Lightning.

Q What was Johnny Lightning?

A Johnny Lightning was a little toy that used to operate on a plastic track and spin around in circles. It was sort of a racing-type toy.

Q And this was in September 1970 --

A Yes.

Q -- that you first heard of it?

A Yes.

Q What was your predecessor's name?

MR. WOLLEN: Excuse me, your Honor. I am not so sure that Mr. Weiss can testify in a competent way as to the problems that Lionel was ~~racing~~ facing.

Are you prepared to put in records of Mr. Weiss relative to the situation between Lionel and Topper in 1970, or are you just relating things that Lionel told him?

MR. DAILEY: The purpose of my examination is to qualify Mr. Weiss with regard to his knowledge gained from personal experience relating to the practices in the toy industry and how that knowledge bears on the interpretation and analysis of financial data, which will come in subsequent to this line of examination.

MR. WOLLEN: Things that Mr. Weiss became aware of relative to what he was doing?

MR. DAILEY: From his own personal business.

MR. WOLLEN: Relative to what he was doing vis-a-vis the Lionel Corporation?

MR. DAILEY: That's correct.

Q What was the name of the senior at Price, Waterhouse who preceded you on the audit?

A The senior was Charles Arden.

Q What did Mr. Arden tell you at that time with regard to the Topper inventory problem which was experienced the year before?

A Well, I don't know whether it was directly Mr. Arden or the staff accountant that was working with him, a Mr. Borkowski, who was in charge of that Lionel audit in 1969 --

Q What is your best recollection?

A I think it was Mr. Borkowski.

MR. WOLLEN: Excuse me. You mentioned the Topper inventory problem. Did you mean a Lionel inventory problem?

MR. DAILEY: That's right, your Honor. Perhaps it was an imprecision of words. It was a Topper inventory problem which Lionel had.

MR. WOLLEN: Now you are talking about 1969?

MR. DAILEY: Mr. Weiss testified that during the course of ~~workeng~~ wozking on the Lionel account in 1970 he had a problem and conversations were brought to his attention.

THE COURT: A problem that Lionel had with its inventory of Topper toys?

MR. DAILEY: Yes.

MR. WOLLEN: You are asking Mr. Weiss what somebody told him about a problem they had had the year before?

MR. DAILEY: That's right.

MR. WOLLEN: I would suggest, your Honor, that that is not competent evidence. That is hearsay.

THE COURT: Well, under the new, relaxed rules I think we can receive that.

Q And what did Mr. Borkowski say with regard to the question of Topper inventory which Lionel had on hand in 1969?

A Well, the only question he had beyond the normal problems that one would have with a normal retail inventory, especially a retail toy inventory -- He said one problem that he had was that there were boxloads of Johnny Lightning in the Lionel inventory.

Q This was Lionel's inventory of Topper?

A Lionel's inventory of Topper.

Q And do you know what procedures Price, Waterhouse took to confirm the accounting of that Topper inventory which Lionel had on hand?

A Well, our main concern with the retail inventory was subsequent to December 25th. We looked at the inventory, and we said, "Look: you have this much inventory on hand, and you either write it down or you can return it," because we just did not believe that there was a substantial market for toys subsequent to December 25th until the following Christmas season, and during that time Lionel would have to present to us some sort of comfort that this merchandise ~~was (a)~~ (a) was being written down or (b) would be returned or credit would be given by the ~~ventor~~ vendor or by the manufacturer for these toys.

Q Do you know what the outcome was with regard to the Topper inventory at hand in Lionel at the end of 1969?

A I believe that substantial credits were issued, but, again, I didn't go into the exact details of the '69 audit. I was more concerned with looking at it from the 1970 audit.

Q When you say substantial credits were issued, issued by whom?

A Topper.

Q All right. Now, turning now to the 1970 audit for Lionel's fiscal year ending December 31, 1970, did any question arise during that audit with regard to Topper inventory on hand at the end of December 1970?

A Yes. Well, it was all inventory again, not only Topper. Basically, we would take the inventory around January 10th of the next year; so, in other words, January

10, 1971, at which time the inventory would be taken, compiled approximately by the end of the month, January 31st, we would get a listing of the inventory on hand, and basically we would evaluate that inventory based upon whether or not it was promotional-type merchandise, non-promotional-type merchandise, whether or not the company had a significant chance of selling it in the subsequent year, whether or not credits would be issued, and generally what we do is sit down with the company and they would tell us, "These are our liabilities," and they would also tell us, ~~that,~~ "We are going to receive certain credits on certain merchandise."

We would then generally confirm accounts payable, which is an extremely unusual audit step, and sent it out to the ~~carious~~ various manufacturers to determine whether or not they had agreed to the credits, the various credits, et cetera, et cetera.

Q During the course of performing this confirmation of payable --

A It would be confirmation of a payable.

Q -- do you recall whether Price, Waterhouse asked Topper to confirm the value of the payables listed on Lionel-Leisure's books?

A Yes; we would.

Q You would. Do you recall whether in fact you did?

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Q Well, we asked them to confirm, yes.

Q Did they confirm?

A I am not too sure whether it was in writing or verbally, but I know they did confirm, and they did confirm to the payable amount on the books.

Q On the Lionel books?

A Yes.

THE COURT: Was there any difference between what you did in connection with Topper and the other --

THE WITNESS: No, sir. We did it for all the --

THE COURT: You are now testifying about Topper.

THE WITNESS: Yes, sir.

THE COURT: At the time, did Topper show any difference? Was there any different --

THE WITNESS: No; it made no difference to us. We did it for all toy manufacturers.

Q Was the inventory amount and the payable amount on Lionel's books net of credits which they felt were due and owing from Topper?

A Yes.

Q And Topper confirmed that the credits would in fact be issued?

A Topper confirmed as to an accounts payable balance. They also confirmed as to certain advertising allowances that were due Lionel. I really don't know whether -- I really don't know which part of this was credits and which part was any of the other, you know, things that Topper might have granted or anybody else might have granted. The only thing that we were particularly concerned with at this time was a payable balance and whether or not that payable balance was fairly stated.

THE COURT: When you say "payable balance", payable by whom?

THE WITNESS: Payable by Lionel-Leisure to the manufacturer, to Topper or any of the other manufacturers.

Q The payable balance being from --

A From Leisure to the manufacturer.

Q And what is the converse of that problem as far as the manufacturer goes?

A I assume a receivable from the manufacturer -- for the manufacturer from the retailer.

Q Well, could it be anything but a receivable?

A Unless they have a new form of accounting, no.

Q Apart from the experience --

MR. DAILEY: Strike that.

Q Apart from the knowledge that you gained peripherally at Price, Waterhouse through the course of auditing the books and records of Lionel-Leisure, have you had occasion to acquire further knowledge concerning Topper Corporation?

A Well, yes. Last year, approximately around, I guess, November or December, I believe, I was assigned to assist the people at Breed, Abbott, the lawyers at Breed, Abbott in reviewing Arthur Young work papers regarding their audit of the Topper 1971 financial statement.

Q Did the scope of your responsibilities also include assisting the lawyers at Breed, Abbott & Morgan in analyzing the financial condition of Topper?

A Yes; it did.

Q In connection with that review, what information did you read and analyze?

A Well, I read all the work papers, or most of the significant work papers, I should say, of Arthur Young. I read the Prospectus. I read the Private Placement Memorandum. I read most of the monthly financial statements issued by Topper. I read their projections.

I read a number of supporting documents for the receivables, aged trial balances. I read a number of documents concerning the warehouse inventory that they had and other miscellaneous things like that.

Q Do you recall reviewing the ~~load~~ Loan Status Work Sheets of Topper?

A I read them.

Q Did you, in addition to reviewing the Arthur Young work papers, also attend the depositions of Arthur Young personnel taken in this proceeding?

A Yes; I did. I attended the depositions of Messrs Cook, Botte Walsh and Zoll, who I think was the senior on the job.

Q Apart from the depositions of Arthur Young personnel, have you also had occasion to review the deposition testimony or excerpts of the deposition testimony of any financial officers of Topper taken in this proceeding?

A Yes. I read the depositions of Schwartz and Rose, and also I read parts of the deposition of Mr. Orenstein.

Q Are you personally familiar with the facts stipulated by the parties in this proceeding as set forth in the request for admissions?

A I read the request for admissions. I am somewhat familiar with the facts.

Q Mr. Weiss, during the course of your experience at Price, Waterhouse, have you had occasion to summarize or cause to be summarized a variety of other financial information?

A Yes; I have.

Q What form would the summaries ordinarily take?

A Well, the -- generally, the summaries that I get involved with are for two purposes -- actually, three purposes.

The first purpose was quarterly financial data that most of my clients would ask me to comment about. The second would be summary information to be included in their annual report, and the third would be summary information to be included in various SEC documents.

Q And how would the summaries ordinarily be portrayed?

A Generally, the summaries for, let's say, a quarterly report, you would have -- it's really based upon what the accounting profession says has to be portrayed. You have your sales; you would have your net income; you would have the provision for taxes, extraordinary items, then a net income number after that, continuing operations data and certain notes to make that information somewhat readable and understandable.

Q Now, prior to your participation in this litigation, have you personally prepared or caused to be prepared any summaries or charts?

A Well, I have prepared summaries and charts, yes.

Q And in what connection were those prepared?

A Well, for a particular assignment I had with the

Metropolitan Transportation Authority and concerning the Long Island Railroad and various information concerning overhead and contribution of overhead.

Q In connection with this litigation, have you personally supervised the preparation of financial summaries of underlying financial information on Topper's books and records?

A Yes; I have.

MR. DAILEY: At this time, your Honor, plaintiffs would offer into evidence a large-scale mock-up of PX 1430.

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THE COURT: Yes. Subject to correction and a motion to strike, that will be received.

(Plaintiffs' Exhibit 1430 received in evidence.)

Q Mr. Weiss, was Plaintiffs' Exhibit 1430 prepared under your personal supervision?

A Yes; it was.

Q What business records of Topper Corporation are summarized on this chart?

A Well, this chart was derived from two separate records. The first one was the Statement of Operations, which was included in the Private Placement Memorandum and in the Prospectus of April 1971, and that would be the actual data submitted.

The projections for 1971 were also included in the Private ~~plavement~~ Placement Memorandum, and this was derived from a projection put out by Topper prior to the completion of the 1970 audit and prior to the, I guess, the Toy Fair.

Q This, then, was the information given to the plaintiffs?

A This was the information given to the plaintiffs, yes.

Q This information did not come from any internal or inside records of Topper Corporation?

A No; it did not.

THE COURT: They were given to the plaintiffs in advance?

MR. DAILEY: Yes. I wanted to make the distinction clear, because Mr. Weiss will be testifying with regard to certain internal records of Topper, and I wanted to make the distinction clear.

Q Did you personally verify that the financial data included in this chart was actually taken from the underlying financial documents?

A Yes. I personally supervised to make sure that that statement was so.

Q Mr. Weiss, will you explain to us why you have chosen the two categories of financial information set forth in this chart, namely, net sales on the one hand and profit or loss from continuing operations on the other?

A Yes.

Q With regard to net sales, why was that chosen?

A Well, I think it best to explain the idea of summary information.

Net sales, basically, as I testified before, is part of the quarterly information. This information is normally included. As far as the case is concerned, we are concerned with the continuing operations of Topper Corporation, and I didn't believe that we would basically be concerned with extraordinary items and special tax problems that Topper might have had in the past because of tax losses.

So the most germane portions to be shown would be net sales and profit and loss from continuing operations. Again, what this chart does is show you the basic financial data that reflect the actual continuing business of the corporation.

Q What are the sales net of?

A The sales are net of returns and allowances.

Q Do you know whether the gross sales information was contained in the Private Placement Memorandum?

A No; it was not.

Q Assuming that the information here is accurate --

obviously, you did not participate in the audit of the Topper Corporation -- but assuming that it is accurate, what conclusions can you fairly draw from the information set forth in Plaintiffs' Exhibit 1430?

A Well, it's pretty evident that as far as net sales go, the company has had a significant increase in its net sales, from $30,292.652 from continuing operations in 1967, to $63,935,619 in 1970, and as we can also see, the projections for 1971 estimated that the company would have further increases in sales amounting to $68,000,000.

When we look at the profit and loss from these continuing operations and add up the sales, we see that the company came from a loss position in 1967 of $582,000 to a profit position in 1970 amounting to $1,464,495, and the projections for 1971 show that the projected net income was going to be $2,690,000.

In all fairness, though, I think it should be pointed out that although this shows a very steady, safe type of increase, the profit and loss percentage in '69 and '70 is not that much different, although sales had increased substantially.

Q Would it be fair to say that based on this information, the profit and loss information, although it did not correlate with the net sales, did give a picture of stability?

A Oh, yes; it did.

THE COURT: Was the fact of such increase projected for 1970, even though the profit was rather negligibly increased from the previous year -- did that cause any --

THE WITNESS: You see, there are two factors that can cause that. Number 1, the increased sales are being increased over a lot of fixed costs, which aren't going to change very significantly. It seems in the latter part of 1970 a considerable amount of their sales came from overseas, so you would have more variable costs, yes, but the fixed costs that they had would be spread over a greater product base.

So it is not too hard to accept the fact that that sort of percentage increase rise is acceptable. It looks pretty acceptable to me.

MR. DAILEY: Your Honor, plaintiffs at this time offer into evidence PX 1431.

THE COURT: What is that?

MR. DAILEY: A chart entitled "Net Sales by Month, Topper Corporation".

(Plaintiffs Exhibit 1431 was received in evidence.)

Q Mr. Weiss, was this chart prepared under your own personal supervision?

A Yes; it was.

Q What business records of Topper are summarized in the chart?

A Well, the records are the consolidated statements of operations included within the monthly consolidated financial statements. In other words, every month Topper put forth financial statements, and these data came primarily from that.

The projections for 1970 came from the same projections that we discussed in the first chart shown.

THE COURT: Any objection to this? It would be subject to the same right to correct.

MR. WOLLEN: No objection, your Honor, subject to that.

THE COURT: All right. It is received.

MR. DAILEY: Plaintiffs also introduce in ~~evidenve~~ evidence Plaintiffs' Exhibit 1366, which is the Topper Corporation projections alluded to by Mr. Weiss and upon which he included the information in that chart.

MR. WOLLEN: No objection.

MR. DAILEY: Plaintiffs' Exhibit 1366 was previously marked as Citibank Exhibit 110 during the course of pretrial preparations.

THE COURT: All right. It is received.

xx (Plaintiffs' Exhibit 1366 was received in evidence.)

Q Mr. Weiss, did you personally verify that the data set forth in the chart were accurately drawn from the underlying financial records?

A Yes. I supervised the verification.

Q Is the information on the chart properly scaled to the underlying data?

A Yes; it is.

THE COURT: Why are there two 1970 items?

THE WITNESS: One is a projection, and one is an actual.

Q Can you explain for the Court and the rest of us the information that is set forth there and summarized on the chart?

A Okay. Basically, what you have here, Topper Corporation is a toy manufacturer. One part of an entire cycle, business cycle, the toy manufacturer and the toy retailer.

The toy retailer, who will sell their product to the ultimate consumer, does most of his business six weeks prior to Christmas, getting extremely active about November 15th. A day or two after Thanksgiving, it's a total bedlam in the toy stores, tailing down around December 24th, and breaking down to almost no business at all in January and February.

In order for the toy retailer to do his business, he must have the product in hand, a tremendous amount of it prior to November 15th, and coming in all through November, so in that context you have to understand this chart.

In January and February, generally, there are very little sales at the retail level, so basically all operations in the toy industry generally stop, and February is a cut-off point, because at the end of February the toy industry traditionally has a toy show.

MR. WOLLEN: Excuse me, your Honor. It seems clear to me that he is talking about the toy industry in general and not Topper specifically. Is that correct?

THE COURT: That is what I understand.

(To the witness:) It is the toy industry generally that you are speaking of?

THE WITNESS: Yes. I am talking about the toy industry as I understand it, in general.

A (Continuing) So that around the end of February we would have the toy show, held here in New York, and this toy show would be where the manufacturers and retailers get together to find out how well they have done in the prior year.

As I have testified before, in the case of Lionel -- and I can speak only of Lionel -- we didn't even know the inventory or the basic success or non-success.

MR. WOLLEN: Excuse me, your Honor. I am willing to listen to Mr. Weiss talk about his experience relative to toy companies and retail companies and his experience through that capacity with wholesalers and manufacturers, but now he is talking generally about what goes on in the toy industry. I don't think he has any expertise in that area at all. I don't know if he is telling things about what goes on at the Toy Fair. I don't believe Price, Waterhouse attends the Toy Fair or anything like that.

THE COURT: Where do you get your expertise in this area?

THE WITNESS: Are you talking to me, sir?

THE COURT: Yes.

THE WITNESS: Well, generally, as part of our audit, as I said before, we would be very concerned with the inventory at year end, and we have generally found as part of our audit that the only way we could ever get final verification of what the payable balance was going to be was at the Toy Fair, because ~~at~~ the Toy Fair, it was explained to me by various people at Lionel-Leisure, was the place where all the manufacturers would get together to discuss the new toy line and what had happened the year before.

So my knowledge comes from people at Lionel-Leisure

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who do attend these toy fairs and from which I get confirmation.

MR. WOLLEN: I don't think that in any way constitutes Mr. Weiss in any way an expert to talk about what goes on.

THE COURT: This is just background information, anyway, isn't it?

MR. DAILEY: Apart from the general background, perhaps we could short-cut this.

Q Mr. Weiss, could you explain for the Court the information that is set forth on PX 1431 with regard to Topper Corporation?

A Well, basically we -- basically, taking the background into consideration, one can see very little activity between January and February in sales.

Q What period is that?

A January to February.

Q Go ahead.

A Now, in the period --

Q What years, by the way?

A I am sorry. 1968, 1969 and as projected in 1970 and actually also for 1970 actual. There is very little activity between January and February.

Subsequent to the Toy Fair, generally you will get very large shipments to toy retailers, and that's reflected here, March to November.

As you can see, in 1968 shipments to toy retailers accounted for 93.9 per cent, and shipments to toy retailers in 1969 accounted for 91.3 per cent.

Q Shipments by Topper Corporation?

A Yes. I'm sorry.

And it was projected by Topper Corporation in 1970 that they would ship 89.8 per cent of their product during the months of March to November, basically.

Again, in accordance with the toy cycle, the retailers had to have a significant amount of their material to sell by November 30th of the Christmas year.

Now, if we compare what has been usual for Topper Corporation in 1968, 1969 and 1970, you could see that Topper Corporation followed this pattern and projected this pattern. However, in 1970, it is very unusual for this company -- for Topper Corporation. They had 21.4 per cent of their sales in December, where they had normally had only 8.6 per cent and 5.3 per cent in 1968, and in the beginning of 1970 they were projecting only 7.5 per cent.

THE COURT: Of what significance is that?

THE WITNESS: Well, again, looking at the toy industry cycle, one would expect that we would have 90 per cent of our sales by November 30th and very little of our sales in December, as was the case with Topper Corporation in 1968 and 1969. However, in 1970 we had 21.4 per cent, or three times the amount percentagewise of sales ~~th at~~ that we could normally expect to have in December of any given year.

THE COURT: Is that a healthy or an unhealthy sign?

THE WITNESS: It depends on what the toy is and when it was delivered. I would say that one would have to question that 21.4 per cent number. It's unusual. It's an abberation. It's not normal for this company, anyway, and one would have to sit down and question why you have a 21.4 per cent shipment figure in November, especially as retail sales are almost negligible in January and February.

Q As to Topper, during the year, Mr. Weiss, during the course of the period March through November, what season or what retail activities would the shipments be directed to?

A It would be directed towards the retailer.

Q And for his sales during what time?

A His sales during the six weeks preceding the Christmas holidays, which would begin approximately November 15th and end December 24th. By that time, we would have all goods sold to his stores if he was going to have any sort of year at all.

Q And the abberation in 1970 stems from the fact that shipments from this toy manufacturer took place subsequent to the time when they could reach the Christmas season?

A Yes; it certainly looks that way.

THE COURT: I am just curious. Why did you have projections in 1970?

MR. DAILEY: Your Honor, this, as you can see, is the pattern in 1968 and 1969.

Q Mr. Weiss, do you know when the projections in 1970 were prepared?

A The projections in 1970 were prepared prior to the audited financial statements of Arthur Young. I assume, therefore, t hat they were also prepared prior to the toy show, since Arthur Young opined on Topper before the toy show took plave in 1971 or 1970.

THE COURT: What use was made of these 1970 figures?

THE WITNESS: Well, the 1970 projections, again, were made for company planning.

THE COURT: But they weren't made part of any Topper financial statements?

THE WITNESS: No.

MR. DAILEY: On the chart, your Honor, I think the first conclusion is that something happened from the time the projections were prepared at the beginning of the year and the end of the year, because there was, as Mr. Weiss has testified, a substantial abberation, and we will get to what inferences can fairly be drawn as to why that happened at a later time.

THE COURT: That was not revealed to the plaintiffs, I assume.

MR. DAILEY: Oh, no. That is the reason why I wanted to take care and point out that the first chart is the only chart that was based on publicly distributed data.

All these other data were internal Topper records, and the projections, of course, were, as Citibank has admitted, furnished to them. They were not in the plaintiffs' possession.

At this time, the plaintiffs would offer Plaintiffs' Exhibit 1432.

THE COURT: Received, with the same conditions previously stated as to the others.

x (Plaintiffs' Exhibit 1432 was received in evidence.)

Q Mr. Weiss, was Plaintiffs' Exhibit 1432 prepared under your personal supervision?

A Yes.

Q What business records of Topper Corporation are summarized?

A Well, the original projection we discussed previous to this was the amount of $68,000,000.

Q That was the original projection at the beginning of 1970?

A Yes, and the actual 51.7 was derived from these monthly statements prepared by Topper.

Q And this is for the period ending -- .

A For the period ending November 30, 1970. The reason we chose this period again is because, for all intents and purposes, for this company, November 30, 1970, can be considered the year end.

THE COURT: Do you have any objection?

MR. WOLLEN: I have no objection to his testimony, your Honor. We have a difference of opinion.

THE COURT: Well, you don't concede the accuracy, but you don't object.

MR. WOLLEN: All my objections to these charts are the same.

THE COURT: They are all subject to correction.

Q Can you explain to us, Mr. Weiss, the basis for your conclusion that for all intents and purposes November 30th was the end of the year for the Topper Corporation?

A Well, again, if you look at this chart, as far as has been the historical record of Topper Corporation, they only had in any December at maximum 8.6 per cent of their sales in December, and even the projections for 1970 from which this number was derived basically anticipated only 7.5 per cent of sales to take place in December, so again, with the flow of the toy market, March to November is a significant period of operations. December is very small. So if you don't make it in November, very often -- at least in this industry, as Topper Corporation is portrayed here -- you just don't make it, and the actual numbers, again, come from the monthly financial statements put out by Topper Corporation.

These are internal financial statements.

Q When you say "put out by Topper Corporation", you mean distributed internally at Topper?

A Yes.

Q To ~~whoever~~ whomever else would be interested?

A Yes. These are Topper-generated statements, and they are unaudited.

Q They are not audited?

A They are not audited. What the chart shows is that of the anticipated $68,000,000 in sales they actually realized 51.7 million in sales. Therefore, they have a short-fall from this projection of 16.3 million.

Q And, again, for the record, what period are we talking about?

A November 30, 1970.

MR. DAILEY: At this time, your Honor, we would like to offer in evidence Plaintiffs' Exhibit 1170, premarked, which is the Topper Corporation Consolidated Financial Statement and Supporting Schedules for the Period Ending November 30, 1970.

THE COURT: These are unaudited?

MR. DAILEY: These are the unaudited ones and constitute the basis for Mr. Weiss' testimony.

Q Mr. Weiss, did you personally verify the underlying data from which this exhibit was prepared?

A Yes.

Q And is the information set forth there accurately scaled?

A It is.

MR. DAILEY: Plaintiffs offer in evidence Plaintiffs' Exhibit 1433.

THE COURT: Received subject to the same conditions stated before.

(Plaintiffs Exhibit 1433 was received in evidenve.)

Q Mr. Weiss, was Plaintiffs' Exhibit 1433 prepared under your personal supervision?

A Yes; it was.

Q And what business records are summarized in Plaintiffs' Exhibit 1433?

A Well, this is a comparison between the original projections which we had discussed previously and the June 1st to November 30, 1970 projections for net sales for this period, June 1st to November 30, 1970.

Q Excuse me --

A The reason --

MR. DAILEY: Let me interrupt at this point, your Honor, to introduce in evidence, or offer in evidence Plaintiffs' Exhibit 673, which consists of revised projections and which previously bore the Citibank Exhibit Number 111. These are part of the data base, again, which is reflected on PX 1433.

THE COURT: If there is no objection, it is received.

MR. WOLLEN: No objection.

xxxx (Plaintiffs' Exhibit 673 was received in evidence.)

Q Could you tell us for what period Plaintiffs' Exhibit 673 projected operations?

A Yes: for the period June 1, 1970 to November -- actually, to December 30 -- 31, 1970. This particular chart picks up that information from June 1, 1970 to November 30, 1970.

The revised projections were prepared some time in July.

Basically, from the chart, you could basically see that ~~basically see that~~ for this period, June 1st to November 30th, they had originally projected 57.0 million dollars.

Q And that original projection was reflected on PX 1432?

A Yes; but this is, of course, for the entire period, January 1st to November 30th, whereas this is a smaller period.

Q That is the original projections we are talking about?

A That's right. It's the original projection that I am talking about.

THE COURT: For a shorter period of time?

THE WITNESS: Excuse me?

THE COURT: For a shorter period of time?

THE WITNESS: Yes, because basically this projection was made up in July for a period June and subsequent.

Q That is an interesting point.

Do you know from the Topper record projections what percentage of Topper sales took place during the period June 1st to November 30th?

A Oh, approximately -- well, better than fifty per cent -- fifty to seventy-five per cent.

The revised projection basically cut the original projection down from 57.0 million to 47.9 million, and still, if you compare the 47.9 million, which is a revised projection, made up in July, which is right in the height of the shipping season, we come out to an actual as of November 30, 1970 for this period of 39.1 million.

So basically there was a short fall in their revised projection, too, of 8.8 million dollars.

Q These were the projections revised in July?

A These were the projections revised in July.

Q And what was the amount of the short fall for this six-month period, June 1 to November 30th, from the original projection?

A 19.9 million dollars.

Q Would it be fair to conclude, Mr. Weiss, that at least as at the end of 1970, Topper was experiencing a rather substantial short-fall in its operations as against what it had projected in January as well as what it revised in July?

A Well, certainly, it wasn't up to expectations.

Q Mr. Weiss, do you have any reason to believe that the financial information set forth here is in any respect misleading or unfairly portrayed a picture of the company with regard to its cash flow?

A No.

Q As of November 30th?

A As of November 30th.

THE COURT: I assume you don't know to what extent, if any, Topper's experiences during this period were differen from those of the toy manufacturing industry in general?

THE WITNESS: I do know, somewhat, only because I did the audit as of December 31, 1970. This was not the greatest year for the toy industry.

MR. DAILEY: Plaintiffs now offer into evidence Plaintiffs' Exhibit 1434.

THE COURT: Received, as before.

(Plaintiffs' Exhibit 1434 was received in evidence.

Q Mr. Weiss, was Plaintiffs' Exhibit 1434 prepared under your personal supervision?

A Yes; it was.

Q What business records are summarized in 1434?

A Well, the projected statements are the January projections that we spoke about earlier. The 1969 -- this is all for the period ending November 30, 1970. The 1969 information represents that $2,315,000 -- All right. It was derived from the consolidated internal financial statements prepared on a monthly basis. The 1970 actual was prepared from the same source but from the 1970 consolidated financial data.

The projection, again, comes from the original January projection.

Now, based on the original projected sales, the company came up with what they anticipated their net income would be, and what we did is, we applied that net income percentage to the actual sales as of November 30th, and we came up with projected net income that they would have had if they had realized their original net profit percentage and applied it against their actual sales, and we came up with a number of 3,955,000 dollars, which, you can see, has a tremendous short-fall, or there is a tremendous short-fall actual to what had been projected under their original net profit estimations.

Q What is the amount of the short-fall?

A $3,766,000.

Q Again, this is where they actually wound up, rather than where they expected to wind up?

A Yes. Topper Corporation, in accordance with its projections, expected a 7 per cent net profit margin. If you apply the 7 per cent to the actual figures, you get that number.

MR. WOLLEN: That is not Topper's figure?

THE WITNESS: No. It is a projected figure It is derived, though, from Topper's projections.

Q Based on their financial information set forth in the January projections?

A In the January projections; correct.

THE COURT: Are your figures based on Topper's projected sales and Topper's projected margin of profit?

THE WITNESS: Yes; they are.

Q Well, let's be clear. That's not quite true, is it?

A The percentage we used in applying it against actual sales was based upon the actual projected sales -- I'm sorry. It was based upon the projected sales and comparing that with what they projected to be their net profit for the year.

That's how we got the percentage. We took that percentage and applied it against the actual sales to determine the profit short-fall from projected to actual.

Q What would the result have been if you had applied this factor to the projected sales for the period ending November 30, 1970, as opposed to actual?

A It would have been -- this projection would have been higher, because instead of applying the 7 per cent against $15,000,000, we would have applied it against $68,000,000.

Q So to that extent this figure is understated?

A That's right. If you were just going to compare projection versus actual on a projected to projected and actual to actual basis, it is understated.

MR. DAILEY: Plaintiffs offer into evidence PX 1435, a schedule entitled Gross Sales Versus Net Sales, Topper Corporation.

xx (Plaintiffs' Exhibit 1435 was received in evidence.)

Q Mr. Weiss, was Plaintiffs' Exhibit 1435 prepared under your supervision?

A Yes; it was.

Q What business records of Topper are reflected on this chart?

A Well, this chart reflects the actual gross sales. The gross sales, as put forth in a letter by Mr. Schwartz to Mr. Conrad K. ~~Sterritt~~ Sterrett.

Basically, in that letter they outline both the gross sales, the returns and allowances, and then they came down to net sales, and this information was taken from the information within that letter.

Q Was the information on the chart also stipulated to by the parties?

A Yes; it was.

THE COURT: Also what?

MR. DAILEY: Stipulated to by the parties.

Q I believe you might point out, Mr. Weiss, that there was one exception with regard to data for 1970, but we can get to that in regular course.

Was the information set forth here accurately drawn from the underlying data?

A Yes; it was.

Q Was it accurately scaled to the underlying data?

A Yes; it is.

Q What conclusions do you draw from the information set forth on PX 1435?

A Okay. You can see what this chart basically shows: that there was a basic breakdown, or there are gross sales and the report that was reported on by Topper is, of course, net sales, as we had discussed before.

The difference is return~~ed~~s, credits and allowances. Now, in 1967, Topper had $5.2 million in returns, credits and allowances, which made up 14.6 per cent of gross sales. In 1968, Topper experienced $6.3 million in returns, credits and allowances out of $14.3 million in gross sales, for a return percentage of 15.3 per cent of gross sales.

In 1969, Topper experienced returns, credits and allowances of $8.8 million out of $62.5 million, for a percentage of 14.1 per cent of gross sales.

Now, we can see that in 1967, 1968 and 1969, returns, credits and allowances made up approximately between 14.1 per cent and 15.3 per cent of gross sales.

In 1970, we had an abberation. We had $19.4 million in returns on $83.3 million in gross, for a return percentage of 23.3 of gross sales, or approximately, percentagewise, 50 per cent higher than had been previously experienced by the company.

2 p.m. wcas

Q This is for the year-end December 31, 1970?

A This is for the year-end December 31, 1970.

THE COURT: That is PX 1435 which is received.

*** (Plaintiffs' Exhibit 1435 was received in evidence.)

Q Again, Mr. Weiss, harking back to the first chart you looked at today, what information was reported in the Private Placement Memorandum distributed to plaintiffs in the Private Placement?

A The information that was in the Prospectus and therefore in the Private Placement Memorandum was, among other information -- but, like, I discussed previously other type financial information, like extraordinary items, was net sales as shown here, and profit and loss from continuing operations as shown here. And this is what was seen by the plaintiffs.

Q But the fact of the gross sales was not set forth in the Private Placement?

A That's right, it was not.

Q Nor obviously the relationship between the two?

A That's correct.

MR. DAILEY: Your Honor, unfortunately, again, because of the time delay, we have some more charts for Topper Corporation, which Mr. Weiss prepared and on which he would be testifying, but unfortunately because of the delay they are not yet available. The ones that are available, however, about which he testified today, do relate to a separate period, namely, up through November 1970. The second set of charts, which hopefully will be ready in a couple of days or so, relate to the period in the summer of 1971, and I think, with the Court's permission, we would like to adjourn Mr. Weiss' testimony for today and recall him when the charts are prepared.

MR. LILLIE: There is no objection to that, your Honor.

THE COURT: I take it you want to save your cross-examination until the testimony is all through.

MR. LILLIE: That is right.

THE COURT: All right. Then you may step down.

THE WITNESS: Thank you.

(Witness temporarily excused)

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MR. BICKS: If you recall, we ended with the testimony of Mr. Weiss showing the shortfall from projections as of November 30, 1970, in both net sales and net profit.

If you recall, the data underlying these charts ties back to the data that was regularly received by Citibank in its role as agent under the Finance Agreement. That was the second area of proof that we introduced by way of documents yesterday.

This was intended as background to the Spring 1971 Program, which will be the subject of testimony today, which involves sales in December, the next month following that.

With regard to the projections underlying these charts, if you recall, in the beginning when we introduced the basic documents reflecting the Finance Agreement, I took the liberty of calling your Honor's attention to particular provisions in the agreements that referred to adherence to projections as a condition to continuance of the loan.

And finally, as further background, it was the Spring Program, if you recall, to go back to one of the first documents we introduced, Mr. Orenstein's letter to shareholders dated ~~September~~ December 17, 1971, that Topper believed was the basic source of its debacle.

So that ties together the proof yesterday and today we begin with the Spring Program. Prior to our first witness I would like to introduce into evidence the basic documents just sketching the general terms and scope of the Spring Program.

I offer documents relating to the background and terms generally of Topper's Spring 1971 Program.

THE COURT: This is in volume 2?

MR. BICKS: Number 2. It's the first volume before you, your Honor, the thick one. May I hand them in without reading the long list of exhibits?

If I may call your attention briefly, if you will turn to the first tab in your book --

MR. LILLIE: Excuse me, your Honor. Just for our sake, can we have the list of exhibits read off?

THE COURT: All right. Let the clerk read the list.

(Pause)

THE COURT: You better have him read it. It will save time in the end.

*** (Plaintiffs' Exhibits 332, 348, 920, 847, 848, 841, 1258, 1259, 852, 915 and 501 received in evidence.)

MR. BICKS: I. I may, your Honor, begin by referring you to Citibank Admissions, which are the first page there, the documents relating, I note that it is not disputed in this case, and I quote, Citibank Admission 79 "The most significant sales period in the toy industry at retail is the Christmas season, traditionally considered to run from Thanksgiving through Christmas."

THE COURT: That's retail.

MR. BICKS: Yes. Then Admission 98, "Because of the lead time required for a manufacturer to distribute toys to the stores in time for the Christmas season, the last effective date they can be shipped to ~~distrebutors~~ distributors, jobbers and certain large retailers to reach the Christmas market is the end of October or early November."

If your Honor recalls, that was the subject of

Mr. Weiss' testimony yesterday.

Then with specific relation to the spring program, Admission 91 recites that "In December 1970, Topper customers were invoiced approximately $16 million of toys on extended credit terms of five to eight months (the "Spring 1971 Program)."

92 recites, and I quote, "At least $11 million of merchandise invoiced under the spring 1971 program was comprised of the Dawn line of toy dolls and accessories introduced at the 1970 Toy Fair."

If you recall, yesterday your Honor heard reference to the Dawn line.

Then Admission 56 sets forth Topper's shipments for various periods and I would ask your Honor to focus on the next to last column of 1970, which shows that for 1970 a total of $41 million of Dawn dolls were shipped. That includes the $16 million on the Program. The size of that quantity is obviously relevant. That's out of a total of $63 million in sales. So $41 million of the $63 million are Dawn, which really focuses the testimony that is to follow.

I would like to call your attention, if I may, to Admission 94, just by way of background here to the testimony, that indeed "During the last four days of 1970, Topper reported at least $6.3 million, or nearly 10 percent, of its net sales for 1970, ~~were~~ with $4 million, or nearly 6 percent, coming on December 31, 1970 (PX 467). These sales represented merchandise aboard ships leaving the Orient on those days."

I suggest to your Honor that New Year's Eve 1970 must have been a rather busy time in Hong Kong harbor, the number of ships moving filled with Dawn dolls.

In terms of the basic terms of the spring program, Admission 95 recited that "In order to induce sales under the Spring 1971 Program, Topper offered customers who ordered prior to December 31, 1970~~,~~ an additional discount of 10 percent."

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MR. BICKS: By way of background, in terms of the problems that customers faced in placing orders of that magnitude the last part of the year, I refer you to Plaintiffs' Exhibit 841, which is a letter from Northern Specialty Sales to the Topper vice president of sales, dated December 21, 1970. This refers to a Spring Program order. The point here is, your Honor, the problem that the distributors faced accepting an order of this size. The first part of that letter I think is worthy of your attention. Northern Specialty Sales through its president advises Topper, "I have been going over the order placed in Las Vegas very thoroughly, and because we find that we are finishing the year with a tremendous carryover, particularly in Topper and Mattel, we physically do not have the space, and I don't think it makes sense to bring in the quantities of merchandise reflected ~~in~~ on this order."

As a result of that kind of feeling on the part of customers, I call your attention next to Plaintiffs' Exhibit 847, which is a letter dated at about the same time from Kiddie City, Mr. Leonard Wasserman. Kiddie City is part of Lionel, about which Mr. Weiss testified yesterday. You recall he testified as to his experience in the Lionel order. The December 18th letter from Kiddie City refers to an order in the amount of $762,000 under the Spring Program, a good portion of the Program, your Honor, roughly 5 percent of it right there, and he says in paragraph 2, "After Toy Fair, when we have had an opportunity to view the new merchandise available for 1971, we will have the following options: (a) an option to return merchandise dollar for dollar for other Topper merchandise; (b) exchange merchandise which will entitle us to retain the additional 10 percent early buy advantage; (c) arrangements will be made through your representative, Mr. Fred Rosen to warehouse part of the merchandise ~~offered~~ ordered."

Those two documents set the background for the Program, your Honor, in terms of difficulties from a distributor's point of view in accepting orders of that size and the essential protection that a distributor insisted upon.

THE COURT: I assume you don't contend that Citibank contemporaneously saw these letters?

MR. BICKS: No, I don't, but I will get to that.

I then call your attention, if I may to Plaintiffs' Exhibit 852. It is a handwritten note, notes taken by Mason Benson, who ~~is~~ was a sales officer in Topper, in a meeting between himself and Orenstein in December of 1970.

Mr. Pierce, who was present at the meeting, has testified that these notes reflect what occurred at the meeting and reflect the sales policy of Topper with regard to the 1971 Spring Program. I call your attention to the words "No risk, no money."

THE COURT: That is, the purchaser has no risk?

MR. BICKS: And then the last three lines, "A chance to make $1,000 on $10,000." That is the 10 percent discount.

The next one, "Every possible protection." And the final line, "Unusual ~~servings~~ savings; no risk category."

THE COURT: Mason Benson was a Topper --

MR. BICKS: A sales officer with Pierce and Orenstein, and the top of the handwritten note reads "Spring Deal Approach."

THE COURT: This is what he was supposed to tell the purchaser?

MR. BICKS: That is right.

Then I called your Honor's attention to the Schwartz deposition in terms of Citibank. Schwartz testified at page 281 -- Schwartz was at that point in time ~~a~~ the Topper Controller -- he testifies being at the Citibank:

"Q What was the purpose of acquainting First National City Bank with that program?

"A We borrowed against receivables."

I would imagine the company wanted to have their blessings on the program. Mr. Schwartz is there testifying to the meeting at Citibank in the development stages of the spring, 1971, program, where they were obtaining their blessings on the program. And following, the Citibank memorandum which refers to October, November and December of 1970, before the program gets underway, Citibank's knowledge of the program, knowledge of the extended dating and how Citibank is going to treat it. Those documents, plus the meetings to get the bank's blessing on the program tie the bank into the early part of the program.

With that background I think we might hear our first witness.

MR. DAILEY: The plaintiffs call Irving Monchik.

IRVING ISSAC MONCHIK, a witness called on behalf of the plaintiffs, being first duly sworn, testified as follows:

MR.DAILEY: Prior to asking Mr. Monchik certain questions, I would like to introduce in evidence eight documents relating to Shepher Distributors, which

BEST COPY AVAILABLE

Mr. Monchik is a part of, and the Topper Corporation.

(The following documents relating to Shepher Distributors and Topper Corporation were received in evidence:)

(Letter from Burt Monchik, Shepher Distributors & Sales Corp., to Topper, dated April 8, 1971, was received in evidence and marked Plaintiffs' Exhibit 1326.)

(United States Customs Shipments schedule of Topper merchandise in transit to Shepher Distributors as of December 31, 1970, was received in evidence and marked Plaintiffs; Exhibit 1450.)

(Letter from Burt Monchik, Shepher Distributors & Sales Corp., to Topper, dated April 1, 1971, was received in evidence and marked Plaintiffs' Exhibit 1327.)

(Letter from Burt Monchik, Shepher Distributors & Sales Corp., to Topper, dated April 12, 1971, was received in evidence and marked Plaintiffs' Exhibit 1328.)

(Letter from Burt Monchik, Shepher Distributors & Sales Corp. to Topper, dated April 14, 1971, with attached copy of said letter with handwritten notations, was received in evidence and marked Plaintiffs' Exhibit 1329.)

(Shepher Distributors & Sales Corp. invoice to Topper, entitled "MEMO - GOOD MERCHANDISE", dated June 3, 1971, was received in evidence and marked Plaintiffs' Exhibit 1330.)

(Shepher Distributors & Sales Corp. invoice to Topper,entitled "RETURN OF GOOD MDSE - MEMO", dated June 4, 1971, was received in evidence and marked Plainiffs' Exhibit 1331.)

(Shepher Distributors & Sales Corp., invoice to Topper, entitled "MEOMO [sic] - RETURN OF GOOD MDSE", dated June 8, 1971, was received in evidence and marked Plaintiffs' Exhibit 1332.)

MR. DAILEY: Your Honor, I have a courtesy copy of these for the witness, and the defendant has received each of these documents together with a list showing the order in which I will treat them, with one exception, and that is the invoice schedule, and I will show it to them if they request when I get to it.

DIRECT EXAMINATION

BY MR. DAILEY:

Q Will you state your present occupation, Mr. Monchik?

A I am a principal in Shepher Sales Corporation and I am actively engaged in sales and purchases.

Q What phase of the toy industry is Shepher Distributors in?

A We are in the distribution end of the toy industry, purchasing from manufacturers and supplying the merchandise to retail discount houses and other types of merchandising , consumer merchandising organizations.

Q How long has Shepher been in the toy business?

A 30 years.

Q 30 years?

A Yes.

Q Have long have you personally been a part of Shepher Distributors?

A 30 years.

Q What is your present position again at Shepher?

A As an officer?

Q Yes.

A I am presently the president of the company.

Q What was your position during the period 1969 through 1971?

A Secretary-treasurer.

Q Will you describe for us, focusing on that period, '69 through '71, what your personal responsibilities were at Shepher?

A My personal responsibilities basically ~~was~~ were purchasing and the controlling of the paying of the obligations that Shepher incurred.

Q As part of those responsibilities did you from time to time have various discussions with toy manufacturers relating to the negotiation of certain inventories which you may have had on hand?

A Constant negotiations with different companies at different times in relation to conditions, whatever they happen to be at the time.

Q Can you give us some idea what customers you sold to during this period?

A Type of customers?

Q Yes.

A Retail stores, department stores and discount stores.

Q When would you typically during this period place your orders for the merchandise you'd buy?

A We were a 12-month a year toy distribution operations. We would constantly buy merchandise on a year-round basis. However,the bulk of the purchasing was done during the toy fair time, which is the springtime of the year, when manufacturers presented their new merchandise and the continuing lines that they did have.

Q Again, during this period what toy manufacturers did you purchase toys from?

A During the period --

Q 1969 to 1971, who were your suppliers?

A Probably, I would say a cross section, most of the major toy manufacturers in the country.

Q Did this include Topper Corporation?

A It included Topper Corporation, which was considered seventh or eighth largest in toy manufacturing in the country at the time volumewise.

THE COURT: What were the others in that category?

THE WITNESS: Ideal Toy Company, Mattel Toy Company, Gabriel Toy Company, Gilbert Company, Kenner Toy Company, et cetera.

Q What was the approximate volume of merchandise which you purchased from Topper during these years on a yearly basis?

A Well, ~~that~~ the day we started about five years prior, prior to 1970, and we started with zero to begin with and then it went up progressively every year from $100,000 to $250,000 growing to $400,000 and then going to $500 thousand and possibly to $650 thousand, and the growth was very rapid in relation to our growth with other companies.

Q During the course of your business dealings with Topper who typically would initiate the placement of an order for merchandise? Topper or Shepher?

A At all times it would start from Topper. They would approach us with a new item or program, whatever, and they would bring it to our attention for our edification and try to interest us in it, and we would get together and work out something.

Q Did there come a time -- I realize it has been five or six years now -- did there come a time toward the end of 1970 when Shepher was approached by Topper and asked to place a rather substantial order of merchandise?

A We were. We were asked to place an unusually large order under special conditions which had existed at that time -- the threat of a longshoreman's strike, an incentive program, getting an additional 10 percent, plus a tremendously aggressive TV promotion.

Q Do you recall approximately what time of the year youwere approached by Topper to place this order?

A Yes, it was the last quarter of 1970.

THE COURT: What did you say about a longshoreman strike?

THE WITNESS: There was a threat of a longshoreman strike and many of the Topper parts originated in the Orient.

THE COURT: The thing was to get it in before the strike?

THE WITNESS: That was the idea.

Q Do you recall approximately the dollar volume of orders which you placed?

A In relation to our type of operation it was a whole year's anticipation probably, which would be about ~~600~~ $600,000, $700,000, in that area.

Q Do you know when the merchandise which you purchased, the six or $700,000, actually arrived at Shepher?

A When it actually arrived?

Q Yes.

A Well, I know it was programmed that we should be billed in the latter part of 1970 and it possibly came in two or three weeks thereafter.

THE COURT: Did you beat the strike?

THE WITNESS: The strike never materialized. The reason why the threat of strike was so strong, the previous year there was a strike, and the following year it seemed like there was going to be another one, and people were very much worried about it.

Q During what period did Shepher intend to sell the merchandise which it purchased in the end of

December 1970?

A Well, the program was that they were going to embark upon a very heavy ~~fairly~~ early spring and summer program and subsequently follow up with a very, very extremely heavy fall program under conditions which were guaranteed, so-called no risk, where anything that was left in stock could be exchanged for a newer merchandise.

(Continued on next page.)

Q At the time they asked you to place the order did they tell you that there would be no risk?

A They indicated that there wouldn't be any risk.

Q Who at Topper Corporation was involved in the placement of this order?

A Our salesman, Nat Shaffir, a fellow by the name of Nat Shaffir. He was directly in -- he was doing business directly, he was our salesman representing the Topper Company.

Q And Mr. Shaffir indicated to you at the time He placed the order that you would be fully protected?

A Yes. I was invited up to the office and they would explain the Program and then Mr. Pierce, who was his superior, came in and explained the Program in further detail, giving us reassurance that we would be fully protected from any overage of inventory.

Q When you say "fully protected from any overage", do you mean any Topper merchandise which you had purchased which you yourself might not be able to sell subsequently?

A That's right.

Q Did Mr. Pierce or Mr. Shaffir explain to you the ways that they would protect you if this event should occur?

A Yes, they did say that they would exchange any merchandise that slowed down in sales with new and current merchandise that they were producing at the time, because they were coming out with their new program for '71, which was supposed to have new items in that program. The nature of the toy business is that every year there are new items by every manufacturer to stimulate their volume.

Q Could you just tell us in terms of the mechanics how an exchange would work?

A An exchange would work in this fashion: I would place an order for new merchandise and I would return the merchandise I couldn't sell or in some cases, I am not saying such was the case with Topper, but in many cases if they felt the merchandise was not of negotiable value that I'd paid for it they would try to give it, sell it to me at a reduced adjusted price.

Q They were trying to --

A That didn't happen in the Topper situation. In the Topper situation we just returned the merchandise for credit.

Q You would get a credit?

A Yes.

Q And that credit would then be applicable to your total relationship with Topper?

A That's right.

Q So if you wanted to purchase merchandise say

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six months later you would have that credit, whatever the amount might be, against that merchandise.

A We could even use that credit against obligations that they had.

Q What would be the amount of the credit?

A The amount would be -- in that area there was some kind of question. The idea was that I was warehousing the merchandise for quite a period of time and the 10 percent which they had offered to me was more or less a warehouse allowance and I'd indicated that I wanted a full credit because the 10 percent warehousing was an expense that I already incurred.

Q Let's see how ~~hwo~~ this works. Let's assume --

A They didn't give me the credit in that fashion, but that's the way I had indicated I wanted it. When I received the credit they gave me a credit less the 10 percent.

Q Less the 10 percent?

A Yes.

Q Mr. Monchik, did there come a time in early spring 1971, approximately three months or so after you received the six hundred, $700,000 worth of merchandise, when you began returning the merchandise to Topper?

A The events that happened ~~happenes~~ as they unfolded, the so-called promotion that was supposed to come about in the spring of '71 never really materialized the way they had programmed it, and I was beginning to get uneasy that I had far too much merchandise at the rate it was moving and then I began to start the ball rolling in relation to returning some of the so-called merchandise which I realized was in excess.

Q This was in April 1971?

A It was three or four months after I had received the merchandise.

Q Before you returned it to Topper did you make any effort yourself to try to sell it to any of your customers?

A Oh, we were selling it and it was selling constantly, but you have to realize that the movement of merchandise was predicated on the amount of dollars they put into TV promotion and it seems that they had cut down on their TV promotion dollarwise, thus causing the items to sell at a much slower pace.

THE COURT: Was this TV promotion in April or May?

THE WITNESS: A TV promotion can be run all year long. It is a question of the price of the item. The items that were involved were low end retailing items, such as an item that sells anywhere from $1 to $5 is considered a low retail seller, and as a rule in the fall the TV merchandise that is sold is anywheres from $5 and up to $50.

Q Mr. Monchik, I call your attention to Plaintiffs' Exhibit 1326, which is in the book before you.

MR. DAILEY: Your Honor, it's also in your book.

Q Would you identify Plaintiffs' Exhibit 1326 for us, Mr. Monchik?

A Yes. That's a Topper item. These were doll clothing outfits.

Q Excuse me. What is the document itself? Is this a business form of Shepher Distributors?

A Yes.

Q This is a debit memorandum?

A This is a debit memorandum which we use when we return merchandise.

Q To get a credit from Topper?

A To get a credit from Topper.

Q Do you know what the merchandise is that you are returning pursuant to this debit memorandum?

A Yes. You are referring to the merchandise that we have here. This is doll clothing outfits.

Q Dawn doll clothing outfits?

A Yes, Dawn doll clothing. Dawn, and they had several other names, but ~~premarily~~ PRiMaRily Dawn.

Q What was the amount of the merchandise that you were returning pursuant to this debit memorandum?

A You want to know in cartons or in dollars?

Q Dollar amount.

A $79,000.

Q I call your attention to Plaintiffs' Exhibit --

THE COURT: You say --

THE WITNESS: This is just the form we use. It's just the form we use.

Q I call your attention to Plaintiffs' Exhibit 1327 in your book.

A 1327?

Q 1327. I skipped over one.

A The next one I have is 1450.

Q The next one should be 1327.

A 2333 --

Q They are tabbed on the side of the pages.

Could you identify Plaintiffs' Exhibit 1327 for us, Mr. Monchik?

A These are -- you want me to identify the amount of moneys?

Q No, just tell us what the document is, if you could, first.

A The document, we returned 3000 cartons of one doll known -- it's a sister of the Dawn doll, which is called Glori doll, and 500 cartons of another doll, which was a friend of the Dawn doll.

Q Is this another debit memorandum?

A Yes, this is another debit memorandum.

Q What is the date of the memorandum?

A The date of that memorandum is April 6.

Q Which year?

A 1971.

Q Could you tell us the dollar volume of the merchandise which you returned pursuant to this debit memorandum?

A The amount involved was $89,964.

Q I call your attention to Plaintiffs' Exhibit 1328. Is this another debit memorandum of Shepher Distributors?

A That's right.

Q Pursuant to this debit memorandum were you also returning additional Dawn merchandise to Topper?

A Additional Dawn merchandise and accessories, which were the clothes.

Q What was the date of this debit memorandum?

A April 12.

Q And what is the dollar volume of the Dawn merchandise which you are returning on April 12?

A $80,000.

Q I call your attention to Plaintiffs' Exhibit 1329. Is this another debit memorandum of Shepher Distributors?

A That's right.

Q What is the date of the memorandum?

A The date is April 14, 1971.

Q What were you returning pursuant to this memorandum?

A Dollars and cents? It was 189 cartons. It could be possibly about $2000. There is no sum of money.

Q There is no sum on that, just 189 cartons?

A Yes. They average about $10 a carton, thereabouts.

Q The product is what?

A The product again is doll clothes.

Q Doll clothes for Dawn?

A Dawn doll clothes.

Q I call your attention to Plaintiffs' Exhibit 1330. Is Plaintiffs' Exhibit 1330 another debit memorandum of Shepher Distributors?

A Yes, these are dolls, these are Dawn dolls, and

Angie dolls and Glori dolls, low end dolls, and this was returned.

Q What was the date of the return?

A The date of the return is July 3, '71.

Q Is that 6/3 or 7/3? It appears to be 6/3 to me.

A It's 6/3.

Q That would be June 3, 1971?

A Yes.

Q What is the dollar volume of the Dawn merchandise which you returned on June 3, 1971?

A $90,000.

Q I call your attention to Plaintiffs' Exhibit 1331. Is this another debit memorandum of Shepher Distributors?

A 1331?

Q Yes.

A Yes.

Q Are you pursuant to this memorandum returning merchandise to Topper Corporation?

A That's correct.

Q What is the date of the memorandum?

A The date appears to be July 7, or thereabouts, '71, in July.

Q How much merchandise are you returning to Topper

Corporation pursuant to that memorandum?

A $60,832.

Q I call your attention to Plaintiffs' Exhibit 1332. Is this another debit memorandum of Shepher Distributors?

A That's correct.

Q What is the date of the memorandum?

A June 8, 1971.

Q Pursuant to this memorandum did you return merchandise to Topper Corporation?

A We did.

Q And what is the dollar volume of the Dawn merchandise which you returned?

A $37,128.

Q These six or seven debit memoranda fall between the period April and early June 1971. Is this the time period when you returned the Dawn merchandise?

A Yes.

Q And was this the Dawn merchandise which you had purchased pursuant to the Spring 1971 Program?

A Practically most of it was that, if not all.

Q You mentioned earlier, Mr. Monchik, made some reference to warehousing.

A Yes.

Q During the course of your dealings with Topper Corporation did they from time to time store merchandise for you in a warehouse?

A Did they store merchandise in their warehouse?

Q In a warehouse for you, or was the merchandise shipped to your warehouse?

A It was shipped directly to us. I know they did have arrangements with some people where they did store merchandise in warehouses, but I never worked it that way. We took it directly into our warehouse.

Q And your offices are located where?

A 2300 Linden Boulevard, Brooklyn, New York.

Q So you are in Brooklyn.

A Yes.

MR. DAILEY: I have no further questions, your Honor.

THE COURT: Any cross?

CROSS-EXAMINATION

BY MR. WOLLEN:

Q Mr. Monchik, is it a fact that Topper's normal payment terms were 2 percent 100 days?

A Normal terms, yes.

Q Could you describe for me what that means?

A It means under normal shipment of merchandise it was understood between the supplier and the buyer that in 100 days from receipt of merchandise payment would be due. That's all it means.

Q With a 2 percent discount for payment in that time.?

A Yes, 2 percent 100 days.

Q Mr. Monchik, you referred to approximately a $600,000 order that you placed with Topper in late 1970.

A Yes.

Q Would you describe that order as optimistic but reasonable?

A Was it optimistic but reasonable? This is a loaded question, and I tell you why.

It was reasonable if they followed the program of what they had promised to do in relation to promoting the merchandise. It was most unreasonable at this particular state in history because they never followed through.

It costs lots of money to promote this particular thing and they may have run out -- I don't know what the financial condition of the company was at the time, but they ran out of something and the momemtum of the merchandise which they had promised to promote just went down to very slow -- almost ~~nimist~~ came to a standstill, and that's the reason why I became uneasy and all this began to take place. The movement of merchandise was not there as they had promised it would happen because of their heavy promotion.

Q I am sorry. I didn't hear your last few words.

A I said because of their heavy promotion we expected to do a certain amount of business every month and it fell way down.

Q Mr. Monchik, you testified before the Securities and Exchange Commission regarding Topper, did you not?

A Yes, I did.

MR. WOLLEN: I point out to the Court that among the transcripts of deposition and other testimony that has been submitted to you is a good portion of Mr. Monchik's testimony before the SEC.

Q Mr. Monchik, did you ever have any contact with First National City Bank concerning Topper?

A Not -- no, not at all.

MR. WOLLEN: No further questions.

THE COURT: Was this operation of Topper's typical of others or was it different from others?

THE WITNESS: Topper, I would say, was an unusual type of operation to the extent that they were more progressive, it seemed at the time, than any of the other so-called more conservative toy manufacturers, and they were aggressive enough to capture a good part of the toy market in fast stages, such as in a five, six year period of time they suddenly were doing sixty, $70 million worth of business per year and projecting possibly $100 million the following year because of the tremendous strides they were making, and several things happened.

They were good for people like ourselves, distributors, because they came out with a franchise situation where they didn't give their merchandise to anybody and everybody to sell. They just put it in every area, geographical area, they had one franchise distributor, and he would handle that particular territory. That was their way of doing business. Most of the competitive manufacturers didn't operate that way. They sold anybody and everybody.

So as a result we had a tendency to favor a company that protected us, and being that the competition was not that keen in their particular merchandise, because in each geographical area one or two or three people carried that line, we could work on a much better markup than we could normally work with somebody else's line, where there were a hundred people selling the same thing. So we had a tendency -- I am giving you the background to give you an idea why we would favor a manufacturer of this kind.

MR. WOLLEN: Your Honor, I might just have one further question in light of what was just answered in response to your Honor's question.

BY MR. WOLLEN:

Q I would like to show you, Mr. Monchik, a copy of Plaintiffs' Exhibit 1333 and ask you if you have ever seen that document before.

A Yes.

Q Could you describe it for us?

A Sure.

Q Please do so.

A We had a verbal agreement in relation to this and we had mild correspondence on it, but when they did not back up their program I began to get uneasy about the whole situation, I wanted something in writing from these people.

Q And this is a result of that?

A That's right.

Q When you say "these people" you are referring to Topper?

A It's indicated there. Mr. Fred Pierce and Topper.

MR. WOLLEN: Your Honor, I offer this into evidence as -- I don't care if it's a plaintiffs' exhibit.

MR. DAILEY: We can offer it as a plaintiffs'

Exhibit.

MR. ~~WILLEM~~ WOLLEN: It's Plaintiffs' Exhibit 1333.

MR. DAILEY: Can I see it, please?

THE COURT: Any objection?

MR. DAILEY: No, not at all.

** (Letter from Frederick C. Pierce to Shepher Distributors re exchange of Topper merchandise, October 26, 1971, was received in evidence and marked Plaintiffs' Exhibit 1333.)

REDIRECT EXAMINATION

BY MR. DAILEY:

Q For the record, Mr. Monchik, will you tell us the date of that letter?

A The date of that letter is October 26, 1971.

Q And what are the provisions of the letter as you understood them?

MR. WOLLEN: I object to that question, your Honor. The letter speaks for itself.

THE COURT: Let me read it first.

I can read the letter.

Q Mr. Monchik, did I understand your testimony to be that prior to the time you received that letter your understandings with Topper with regard to exchange of merchandise were oral?

A Were oral, that's right.

MR. DAILEY: I have no further questions.

THE COURT: But that letter expresses the arrangement that had been existing all the time?

THE WITNESS: That's correct.

THE COURT: You just wanted it in writing?

THE WITNESS: I was getting uneasy, there was too much involved, and I felt I was getting involved in something that was giving me indigestion, and here I am now. I am in the midst of my heavy toy buying season now and I have to be here because this gets priority.

MR. WOLLEN: No further questions, your Honor.

THE COURT: You may step down. Go buy some toys.

THE WITNESS: Thank you, Judge.

(Witness excused)

MR. DAILEY: Your Honor, plaintiffs call Mr. Lawrence Ades of Pensick & Gordon.

LAWRENCE S. ADES, called as a witness by the plaintiffs, having been first duly sworn, testified as follows:

MR. DAILEY: Your Honor, I would like to follow the same procedure with Mr. Ades and offer into evidence at one time the eleven exhibits relating to Pensick & Gordon and Topper Corporation, which will be the subject of Mr. Ade's testimony.

(Topper memorandum from Jerry Gross to Frederick C. Pierce re redating and exchanges, December 8, 1969, was received in evidence and marked Plaintiffs' Exhibit 1342.)

(Pensick-Gordon interoffice memorandum from Larry Ades to files re arrangements for excessive Topper inventory, March 9, 1970, was received in evidence and marked Plaintiffs' Ehxibit 1343.)

(Letter from Pensick-Gordon to Topper re inventory adjustments, September 25, 1970, was received in evidence and marked Plaintiffs' Exhibit 1344.)

(Topper memorandum from Jerry Gross to Frederick C. Pierce re inventory adjustments for Pensick-Gordon, November 7, 1970, was received in evidence and marked Plaintiffs' Exhibit 1345.)

(Letter from Frederick C. Pierce to Pensick-Gordon re inventory adjustments, March 4, 1971, was received in evidence and marked Plaintiffs' Exhibit 1346.)

(Letter from Lawrence S. Jaffe, Pensick &

Gordon Inc., to Jerry Gross, April 20, 1971, was received in evidence and marked Plaintiffs' Exhibit 1349.)

*** (Letter from Frederick C. Pierce to Larry Ades of Pensick & Gordon Inc. dated December 9, 1970, was received in evidence and marked Plaintiffs' Exhibit 888.)

*** (Letter from Frederick S. Pierce, Topper Corporation, to Pensick & Gordon Inc., dated March 17, 1970, re $244,337.71 in redated receivables, was received in evidence and marked Plaintiffs' Exhibit 1451.)

*** (Letter from Frederick C. Pierce, Topper Corporation, to Larry Ades, Pensick & Gordon Inc., dated January 20, 1971, was received in evidence and marked Plaintiffs' Exhibit 1452.)

*** (Pensick & Gordon Inc. memorandum to Topper Corporation re returns, December 23, 1971, was received in evidence and marked Plaintiffs' Exhibit 1454.)

*** (One-page handwritten memorandum from John E. Vogt to Julius H. Schwartz, dated August 18, 1971, was received in evidence and marked Plaintiffs' Exhibit 1223.)

DIRECT EXAMINATION

BY MR. DAILEY:

Q Mr. Ades, I hand you a courtesy copy of each of the documents we will ask you to testify concerning this morning.

Mr. Ades, what is your present occupation?

A I am president of Pensick & Gordon, division of W. R. Grace.

Q And what is the business of ~~Pensich~~ Pensick & Gordon?

A Wholesale toy distribution.

Q How long has it been in the wholesale toy distributing business?

A 51 years.

Q How long have you personally been connected with Pensick & Gordon?

A Approximately 30 years.

Q 30 years?

A What is this, 19-- 1946 I started. Where are we now? 30 years.

THE COURT: It hasn't been a division of Grace all that time.

THE WITNESS: No, just the last two years.

Q Pensick & Gordon was acquired by Grace in '74 or thereabouts?

A '74, January.

Q Focusing on the period 1969 through 1971, what were your responsibilities at Pensick & Gordon?

A I was president of the company.

Q As president what did you do? I mean on a daily basis, with ~~Pensich~~ Pensick & Gordon.

A Well, I ran the company.

Q As part of your responsibilities were you involved in the decision to select and purchase toys from manufacturers?

A A portion of them, yes. Overall and responsibility in total, as president of the company I have that.

Q As part of your responsibilities did you from time to time during this period have various negotiations with toy manufacturers relating to any problems you might have with them?

A Yes.

Q What toy manufacturers did Pensick & Gordon purchase from?

A Virtually all of ~~the~~ them.

Q Was Topper one of them?

A Yes.

Q Do you recall when Pensick & Gordon began purchasing toys from Topper?

A I can't give you the exact year. It was the second year that they distributed toys through the toy trade.

Q Would this be approximately '67, '68?

A I couldn't tell you.

Q Do you recall whether you were purchasing merchandise from Topper during the period 1969 through 1971?

A It's hard for me to remember each year as we go back, but apparently that is the case, yes.

Q We understand. It's been more than six or seven years now.

Again focusing simply on the period 1969 through 1971, did there ever arise an occasion when Pensick & Gordon had an excess amount of Topper inventory which it had previously purchased and was itself unable to sell?

A Yes.

Q I call your attention to Plaintiffs' Exhibit 1342 and to the second page of the exhibit.

Calling your attention to the second page of the exhibit, was this a memorandum which you prepared?

A Is this the December 8, 1969 you are referring to?

Q Right. There are two memoranda and the second one appears to be on Pensick & Gordon interoffice correspondence, the second page.

A I only have one page.

Q This is the page I am referring to.

Was this a memorandum which you prepared?

A Yes.

Q I call your attention to the second and third paragraphs, which read "Topper will ship us in December the balance due on the Johnny Lightning cars, approximately 1200 cartons.

"They have agreed that at the Toy Fair or shortly therafter ~~whould~~ should we have any excess inventory left, i.e., 150 cartons or over, they will:

"1. Exchange this ... for 1970 cars.

"2. Redate any of this inventory to the terms at which we have bought at Toy Fair."

MR. WOLLEN: I think you left out the word "would."

Q "Which we would have bought at Toy Fair."

MR. DAILEY: Thank you, Mr. Wollen.

Q Mr. ~~Aids~~ Ades, does this memorandum accurately reflect an understanding which you had with Topper with regard to the Johnny Lightning toys?

A You are asking me to go back to 1969, but if I wrote this memo, this was the understanding.

Q I call your attention to Plaintiffs' Exhibit 1343, which for the record is a Pensick & Gordon interoffice correspondence dated March 9, 1970.

Mr. Ades, did you prepare this memorandum?

A Yes.

Q Would you review it?

A Wait a minute. The November 17th?

Q Would you just read over the memorandum, would you just read the contents of the memorandum to yourself.

A You want me to read the November 17 one also? Is that what you are referring to?

Q Yes, please.

THE COURT: This term "redate", that obviously is a term of art. What does it mean?

THE WITNESS: Which paragraph are you referring to?

THE COURT: It says "redate" to October 10. What does that mean?

THE WITNESS: That meant that we didn't have to pay for the merchandise at the original due date.

THE COURT: That means as though it had been purchased on October 10?

THE WITNESS: Or it would have been purchased later than the original purchase so that it would then be due October 10.

Q Was the Topper merchandise which is the subject of the two memoranda denominated Plaintiffs' Exhibit 1343, was this merchandise which Pensick & Gordon had purchased from Topper in 1969?

A I will have to figure this one out.

I would assume that for the most part -- there might have been some 1968 goods in there, but I would say primarily 1969.

Q It could be '68 or '69?

A Yes.

Q It would not be 1970 purchases?

A Well, the memo is 1969.

Q Yes, that's right, and it is attached to a memorandum dated March 9, 1970. These were understandings which you had with Topper at the end of 1969 which were memorialized and attached to a memorandum dated March 9, 1970, but which related to your 1969 purchases from Topper?

A Start over, say that again.

Q The subject matter of the two memoranda relates to 1969 purchases from Topper, does it not?

A Yes.

Q I call your attention to paragraph 2 on the second page of the memorandum dated November 17, 1969, which reads "Topper has guaranteed that Pensick & Gordon will take no markdowns on the above mentioned inventory, i.e., if items become distress or not saleable at the regular price, Topper will credit Pensick & Gordon down to a price that will enable the merchandise to be moved."

Could you tell us what is involved here?

A There would be various ways this would be handled. If they had a product that perhaps lets assume we paid $9.50 for. They would sometimes go to a large retail operation and if the item did not sell at the original cost and selling price they would offer it at a reduced price. Frequently they would have us bill it and they would credit us with the difference, to get it out of our warehouse.

Q I call your attention to paragraph 4, which reads "In the event there are one or more items in the final inventory of extremely large quantity or bulk, Topper agrees upon request from Pensick & Gordon to physically remove all or a portion of said merchandise."

We have had redating in paragraph 1, some form of markdown and credit in paragraph 2. What was the type of adjustment involved in paragraph 4?

A Well, we have a physical problem in utilization of our warehouse space. So within reason we would keep the merchandise until it could be disposed of by either Topper or whatever other means. However, if the thing ~~gout~~ got out of hand and it was just tremendous bulk of one or more items that we couldn't physically handle or didn't want to keep because of limited space they had to take them out, get them out.

am

Q In terms of the mechanics of the transaction what would be involved? Is there a credit to you for the amount of merchandise that was removed?

A Which transaction?

Q The transaction reflected in paragraph 4.

A It could happen one of three ways. The one that I mentioned to you, where they would negotiate a deal, we might invoice the customer at the new lower price, receive a credit. I believe there were circumstances where they sold the merchandise direct or would invoice the retail customer direct, and then we would receive a credit for the purchase that we had paid; and then a third was that they had a warehouse in Clearfield, Utah, a public warehouse there, and I believe in certain instances we just shipped the merchandise back to Clearfield under their account and we received credit.

Q The merchandise you shipped back to Clearfield, Utah, was merchandise you yourself were unable to sell?

A Yes.

Q I call your attention to Plaintiffs' Exhibit 1451. Is that a confirmation on the redating which was reflected in Plaintiffs' Exhibit 1343?

A Toy Fair was on in that period. This is March 17th; I assume this is a follow-up of the March 9th.

Q Could you tell us what your understanding was with respect to the redated merchandise in the amount of $244,000?

A There are so many deals, I can't remember this one precisely.

Q This would have been merchandise which you could not have sold in 1969 and it was redated to you in 1970?

A Right.

Q I call your attention to 1344. Is this a copy of a letter which you wrote to Mr. Pierce on September 25, 1970?

A It would appear so. Why is my signature not on it?

Q It appears to be a copy, a Xerox copy of a carbon copy. This was a letter which was submitted by Pensick & Gordon to the Securities and Exchange Commission, produced under the Freedom of Information Act.

I call your attention to paragraph 1, which reads, "On October 10th we will pay you approximately $100,000 plus the inventory carryover net of credits of approximately $203,000 for a total in the neighborhood of $303,000."

Do you know what the credits of $203,000 referred to in this letter relate to?

A I could not remember at this point. I would assume they refer to the previous carry-over inventory that was subsequently adjusted during the year.

Q Is the redated inventory the $244,000?

A In all probability it was.

Q You subsequently received a credit of $203,000 against this?

A I can't swear to it. It would appear to be.

Q But the letter does indicate, whatever the reason might be, Topper did issue a credit of approximately $203,000?

A That is what it says. I can't remember 1970, obviously.

Q I call your attention to Plaintiffs' Exhibit 1345, a Topper Corporation document. It is a memorandum, I believe, from a gentleman named Jerry Gross, to Fred Pierce, and it relates to Pensick & Gordon, and I have no reason to believe that you have ever seen this, and this reads in essence:

"We agreed --" we being Topper -- "at our meeting in Las Vegas to remove from Pensick, Gordon warehouse any inventory in excess of $100,000."

By the way, the date of the memorandum is

November 7, 1970.

"The $100,000 figure was the maximum inventory that Pensi . rdon was responsible for as per our Toy Fair deal."

Mr. Ades, do you recall the transaction which apparently is referred to in this letter with the understanding that Pensick & Gordon would only be responsible for $100,000 in its purchases?

A Can you be more specific on this?

Q Do you recall some time during 1970 having an agreement with Topper that you would only be responsible for $100,000 of the total amount of merchandise which you purchased?

A Again, I can't remember the year, but if this is the memo, this was the situation.

Q I call your attention, Mr. Ades, to Plaintiffs' Exhibit 1452, a letter from Fred R. Pierce, of the Topper Corporation, to Larry Ades, dated January 20, 1971. Do you know who Mr. Pierce was?

A Oh, yes, he was vice president of sales at Topper.

Q Did you from time to time have various negotiations with Mr. Pierce?

A Yes.

Q Will you read the letter to yourself?

A I have read it.

Q I call your attention to the second paragraph of the letter:

"Our agreement for 1970 was that we will give you reshipping instructions in case our inventory is in excess of $100,000."

Will you tell us what the reshipping instructions were?

A Those were the same three things that I mentioned to you earlier, methods of getting the merchandise out of our warehouse.

Q Merchandise which you were unable to sell?

A Yes.

Q I call your attention to the last paragraph of the letter, which reads:

"By April 1 of 1971, we will either give you the aforementioned shipping instructions or, if it is mutually agreeable, work out with you certain advertising adjustments so that you can keep this merchandise. This will be done at your option."

A The word "advertising" is a questionable word. Again, assuming we paid $9.50 and they said we are now willing to credit you down to a cost of $3, it might have been in our interest at that point to forego our guarantee on that portion of the inventory and buy it outright from Topper or conclude that portion of it.

Q And the advertising adjustment, as you said, a questionable word, was the credit that you got between $9.50 and $3?

A Under those circumstances, that is the only way we would have kept the merchandise was at a reduced price, yes.

Q Then you would try to sell it at a reduced price?

A Yes, it was then our responsibility.

Q And that was in lieu of returning it?

A That is right.

Q I call your attention, Mr. Ades, to Plaintiffs' Exhibit 1346 --

A Can I ask you a question? Are we moving chronologically here, because I am losing track of the years.

Q We are in early 1971 now.

A Okay.

Q Plaintiffs' Exhibit 1346 is a Topper Corporation letter from Fred C. Pierce to Mr. Lawrence S. Ades, Pehsick & Gordon, dated March 4, 1971?

Will you review the letter, please? I call your attention to the second paragraph, which says, "In consideration of Pensick & Gordon, Incorporated's Toy Fair order, Topper is granting a special Toy Fair advertising allowance of $149,300.00. Topper also agrees that they will redate any inventory existing on December 31, 1971, in excess of 10 per cent of Pensick & Gordon net 1971 purchases. Pensick & Gordon will not be obligated to pay any such excess until such time as the merchandise is disposed of at no financial loss to Pensick & Gordon."

Was this your understanding as set forth, is paragraph 2 your understanding as to the redated merchandise?

A Which redated merchandise?

Q The letter indicates that Topper has agreed with you that if you have any leftover inventory at the end of 1971 they will redate it for you, but that you will not be obligated to pay for any excess until you dispose of it.

A That is correct.

THE COURT: Is there anything to the fact that the previous letter was addressed, "Dear Larry," and this one is addressed, "Dear Mr. Ades"?

THE WITNESS: I wondered about that myself. No, I have no idea.

Q I call your attention to Plaintiffs' Exhibir 1349, which is a letter dated April 20, 1971, from Mr. Lawrence S. Jaffe, of Pensick & Gordon, to Jerry Gross.

Who is Mr. Jaffe?

A Who is he presently? Is that your question?

Q Yes.

A He is vice president of finance of Pensick & Gordon.

Q I call your attention to the second paragraph of the letter, which reads, "Jerry, this whole situation is ridiculous. Last week I requested a copy of our account as it appears on your company's books for which I have yet to receive a reply. You have assured us that all of the 'garbage' pertaining to last year has been taken care of and that it would not repeat itself for 1971."

Do you recall the circumstances that Mr. Jaffe is referring to in this letter?

A No. I can only surmise. Our fiscal year would end on January 31st and we want to be sure we had everything reconciled.

Q Do you know what Mr. Jaffe's reference of the word "garbage" is to?

A We were going crazy trying to get our account payable to look like Topper's account receivable.

Q The "garbage" then would be the Topper inventory?

A No, no, he is trying to get the paper work done.

Q What was the problem of reconciling your account with theirs?

A This was not my area of responsibility. I can't answer that.

Q Mr. Ades, again I realize it has been some time, but going back to the end of 1970 did there come a time in the period November or December, 1970, when someone from the Topper Corporation approached Pensick & Gordon concerning the placing of an order under the Spring 1971 Program?

A You really need a chart of Topper for me. Could I ask a couple of questions? Was this the container program on the dancing doll?

Q Right. Do you recall that program?

A Yes.

Q What do you presently recall about it?

A We passed that program, either passed it or bought a very small quantity. It involved containers out of the Orient, where you were invoiced and took title as the container left the port in the Orient.

Q When you say you passed it, you mean you did not participate in it?

A Yes, just buying some.

Q You did not participate to the extent Topper wanted you to participate?

A That is correct.

Q Can you tell us the reasons you did not participate?

A Very simply, I could not have those kind of liabilities on my balance sheet, and our fiscal year ends January 31. That was one of my primary reasons. I could not have that on my balance sheet for my fiscal closing and I passed it.

THE COURT: Not everything is run by computers.

THE WITNESS: Well, accountants have something to say about what you do today, too.

Q You have gone over in the exhibits, Mr. Ades, certain arrangements you had with Topper relating to excess inventories in 1969, 1970. Do you recall whether these arrangements carried over in 1971?

A Which was 1971? What happened in 1971? What exciting event occurred.

Q We went over arrangements with regard to the years 1969 and 1970 and we have seen through your correspondence that from time to time you had excess Topper inventories and you entered into certain agreements with them to dispose of the inventories by returning it, reshipping it, or keeping it, taking advertising allowances.

My question is whether you recall whether these types of arrangements carried over into the year 1971?

A Didn't we say that in one of these letters?

Q Plaintiffs' Exhibit 1346?

A 1346 states that.

Q I was unclear whether that related to 1970 or 1971. Do you read that prospectively?

A Redate any inventory. "Topper also agrees that they will redate any inventory existing on December 31, 1971 in excess of 10 percent of Pesnick & Gordon net 1971 purchases."

Q I call your attention to Plaintiffs' Exhibit 1454. Could you identify this document for us, sir?

A That is one of our standard form of debit memo to a vendor.

Q Can you tell from looking at the document what circumstances gave rise to a debit memorandum?

A I can't tell you specifically. I would assume that being the end of 1971 would have brought us into the 10 percent factor referred to in the previous letter, which was our agreement.

Q What was the 10 percent factor?

A That our inventory carryover at the end of the year would not exceed 10 percent of our purchases.

Q Anything over 10 percent you could return or get some other allowance or adjustment?

A Yes.

THE COURT: You were a wholesaler?

THE WITNESS: Yes.

THE COURT: Anything you had on December 31st you wanted to get rid of?

THE WITNESS: There was a very limited market at that point.

Q Do you recall, Mr. Ades, some time during the summer of 1971 cancelling a rather substantial order of Topper merchandise which you had previously placed?

A Cancelling an order I had placed? I don't recall specifically.

Q I call your attention to Plaintiffs' Exhibit 1223, which is a Topper memorandum of Mr. Vogt to Mr. Schwartz, which reads, "Value of orders booked ~~had~~ has decreased from the 7/31 figure $52,553,569 as of 8/17/71. This decrease was caused in part by the cancellation of the stock control order of Pensick & Gordon for $515,802."

Does that refresh your recollection, sir, with regard to my previous question?

A I can't remember that.

THE COURT: What did you say?

THE WITNESS: I cannot remember this.

MR. DAILEY: I have no further questions.

MR. WOLLEN: Might I inquire whether Plaintiffs' Exhibit 888 has been introduced in evidence? It was on the plaintiffs' list, but I did not hear it referred to.

THE CLERK: It has been received.

CROSS-EXAMINATION

BY MR. WOLLEN:

Q Mr. Ades, I will hand you Plaintiffs' Exhibit 888, which has been received in evidence, as you if you remember that letter.

A What is your question, sir?

Q Do you remember it?

A No.

Q To the best of your recollection, does it accurately reflect the understanding referred to?

MR. DAILEY: Your Honor, I object. The witness has testified he doesn't remember.

THE COURT: He said he doesn't remember.

Q You have no recollection of this letter at all?

A Well, it's talking six years ago.

Q You remember the other letters that counsel questioned you about.

THE COURT: He says if that is what it says it must be so. That's a typical answer.

Q Mr. Ades, did you have any contacts with First National City Bank concerning Topper?

A I received a phone call two weeks ago from an attorney who I believe said they represented someone in the Topper case. That could have been --

Q Let me limit my question to prior to January 1, 1973.

A Prior to January 1?

Q '73.

A Did I have --

Q Any contacts with First National City Bank concerning Topper, to the best of your recollection.

A No.

MR. WOLLEN: No further questions, your Honor.

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MR. BICKS: These documents reflect Topper's practice of returns and exchanges about which you have heard testimony.

With regard to Citibank's knowledge thereof, I call your attention to the extract of Garvin's testimony before the SEC which appears immediately behind your third yellow tab. Page 51 of that transcript, beginning at line 19, Mr. Garvin is questioned and answered as follows.

THE COURT: He was being quested by SEC counsel?

MR. BICKS: That's right. Mr. Garvin is a senior vice president at this point in time of Citibank, senior to Mr. Waldman. I was speaking in terms of the Citibank hierarchy, not ultimately in terms of worth, obviously.

I refer you to page 51, beginning at line 19:

"Q Did you ever discuss with Mr. Waldman rights given by Topper to its customers to return goods?

"A Other than it is common in the marketplace.

"Q Had Waldman indicated to you that is is common in the marketplace?

"A Waldman and other lending officers.

"Q What other lending officers?

"A I mention ~~Matell~~ Mattel for one.

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"Q Mattel ~~Matell~~?

"MR. LILLIE: Other lending officers?

"THE WITNESS: Other lending officers. I don't know what --"

THE COURT: Mr. Lillie is SEC counsel?

MR. BICKS: Mr. Lillie is here. He was accompanying Mr. Garvin on that occasion.

"Q I am asking what are the names of those other lending officers.

"MR. LILLIE: If you remember.

"A We have 400 of them.

"Q Any of them.

"A Specifically on this particular problem?

"Q No.

"MR. LILLIE: Where any other lending officer" ---

THE COURT: I assume that was "were."

MR. BICKS: That's right. "Where any other lending officer ever mentioned to you that was a common practice in the industry.

"A The answer is yes and I can't say who it was.

"Q Other than Mr. Waldman.

"A Mr. Waldman and the account officer of Mattel ~~Matell~~ no doubt talked about it."

THE COURT: Who is Mattel ~~Matell~~?

MR. BICKS: Another toy company. ~~Matell~~ Mattel is one of the suppliers that you heard --

THE COURT: And they also are financed by the bank?

MR. BICKS: Apparently. I know of nothing on that score other than what appears in the transcript, your Honor.

"Q Do you know whether ~~Matell~~ Mattel has given its customers the right to return merchandise for cash or credit?

"A I do not know.

"Q Well, was it ever indicated to you that they did in fact give customers that right?

"A As I indicated before, I have been told by the lending officers ~~the~~ that deal in the toy business, that it is common market practice to make sales and at the end of the Christmas season frequently some of the merchandise is returned, and therefore you can look at it as a consignment rather than an outright sale."

Now, the only other reference --

MR. WOLLEN: Your Honor, might I inquire whether the page that was handed to you includes the entire page 53 or stops where Mr. Bicks stopped reading.

THE COURT: The page is physically there but

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it's crossed out.

* * * * * * * * * * * * * * * *

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MR. BICKS: That's right.

So much for the practice of the ~~change~~ exchanges and returns from Citibank's point of view. I would like to call to your attention, and since it is rather important, read several paragraphs from the deposition of Mr. Frederick Pierce, again at page 14.

Mr. Pierce, as the testimony has indicated, your Honor, was Topper's vice president of sales at that point of time. I think rather than taking you through all the documents, his testimony as to the general practice of exchange will suffice and place all the documents in a meaningful context.

I would like to begin, if I may, at line 23, the bottom of page 14.

THE COURT: My Pierce deposition starts at page 150.

MR. BICKS: This is in your book following marketing practices, returns and exchanges.

THE COURT: That's what I have. The Pierce deposition comes right after 1112.

MR. BICKS: Comes right after 711. It comes after 711, your Honor. I think you may be in the wrong section.

THE COURT: Yes.

MR. BICKS: "Q How did rights of exchange fit into the spring or '71 program?

"A The rights of exchange came up I believe with the Kresge Company.

"Q That was prior to the spring '71 program though, wasn't it?

"A Well, the thing that sticks in my mind is the

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presentation was made by Mason Benson to Kresge and he came back and said, 'You know, they were willing to go along with the program but if they were wrong in their selection of merchandise they wanted to be able to exchange that merchandise for some other merchandise,' and Mr. Orenstein and I believe Mr. Rose worked out the wording of the agreement that they wanted and I think that was the first instance of right of exchange.

"Q But you as I think your title was vice president of sales recognized the right of exchange in terms of that program at that time?

"A No, only at that point it was only as far as Kresge was concerned.

"Q When did the situation change?

"A When we made presentations to our major distributors and the same basic question came up, you know, if they are buying extremely large quantities of merchandise which were promarily based on our availability, that if they bought too much of one doll could they exchange it for another doll at some later date, and I went to Mr. Orenstein and discussed it with him with other people, but I am not sure who they all were, and he agreed that on that basis if in fact they were wrong, if you will, at that point, try to look far in advance that they could exchange dollar for dollar merchandise.

"Q As long as that other merchandise was part of the '71 line, that was part of it too, wasn't it?

"A The '71 line, yes."

I would like, if I may, to skip to page 18, line 2:

"Q On the right to exchange point, before we leave that and go into the detail of particular customers, I believe you indicated the situation had arisen first with Kresge and then following official presentations during November of 1970 to various customers the granting of rights of exchange to other customers appeared worthy of consideration in terms of the program, at that point you brought the matter to Mr. Orenstein.

"A Right.

"Q Could you tell us just briefly what the substance of that conversation was, your conversation with Mr. Orenstein on the subject?

"A Well, basically I brought to his attention the fact that our customers felt similarly to the attitude of Kresge, that if they ~~were~~ are going to place these large quantities that they wanted to be able to vary within the available '71 merchandise products if they were wrong in the type of position they were taking, which was extensive.

"Q What did he say?

"A He thought that was a reasonable request after some discussion.

"Q And following that discussion did you feel authorized to proceed on the basis of granting such rights in these circumstances?

"A I believe that we initially discussed a list of the accounts that could possibly be involved in this exchange due to their size and then in the larger accounts that we did business with and then beyond that he basically told me to use my own judgment.

"Q Was any particular form of ~~agreement~~ arrangement discussed at that time?

"A Yes, the form basically was that we would assure the customer that if he had a question of exchange that he would be allowed to exchange the merchandise for other available merchandise.

"Q And without pinning you down as to a particular day or a particular week, what was the approximate time frame in which this discussion took ~~paace~~ place with Mr. Orenstein?

"A Strictly on a logical basis it had to be about the first part of November.

"Q Of 1970?

"A Yes.

"Q Prior to the making of major commitments by customers under the spring '71 program?

"A After some initial presentations had been made but before the major commitments were made.

"Q I didn't mean to limit you by my paucity of knowledge in terms of the questions I have asked you. Are there any other essential ~~terms of~~ elements OR major ~~limits~~ elements of the program which you think for the sake of completeness we ought to have on the record?

"A The only obvious fact that came up was subsequent to that the customers requested letters confirming the exchange agreement. As I indicated originally it was Kresge that requested it in writing. I believe the next time it came up was Pensick & Gordon, who said, 'Fine, I understand the exchange and that's fine, but I want it in writing.' It came back to me through my sales force and I went to Mr. Orenstein and said, 'Pensick & Gordon want it in writing,' and he said, 'That's no problem, write the letter, check it with Jack Rose,' and that's precisely what happened."

THE COURT: Who again was Jack Rose?

MR. BICKS: He was the chief financial officer of Topper.

"Q That's what you did?

"A Right.

"Q And your recollection is that the Pensick & Gordon letter you checked with Mr. Rose.

"A Yes. I also believe he reworded it. I have obviously since seen the letter and it doesn't appear to be my normal day-to-day language.

"Q And following that check with Mr. Rose with regard to one customer, namely, Pensick & Gordon, did you utilize essentially the same form of language in other letters when they were requested by customers with regard to rights of exchange?

"A Yes."

Thus far, your Honor, we have had the general terms of the Spring Program and the policy, that no risk, no money; second, consessions generally; third, returns and exchanges; fourth, I introduce documents relating to another form of Topper concession, namely, what has been referred to as a promise of protection.

THE COURT: Promise of protection?

MR. BICKS: Promise of protection. You heard Mr. Monchik I think it was ~~refer~~ Referred to "We will be protected." At this point I introduce documents with other customers referring to the same assurance as another example of the type of consession made by Topper in connection with the spring '71 program and thereafter.

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MR. BICKS: Your Honor, there are just two more categories of documents and then we will complete this. If I may, I think they might be more meaningful immediately after the testimony of Mr. Greenman, who will be appearing -- I think you said at two we should be back.

Immediately following Mr. Greenman I would like to put in documents on the category of warehousing, Topper's warehousing practices, and redating practices, and that would complete, I would say, 95 percent of the documents in the case.

THE COURT: All right. I assume that what you are developing here is the general proposition that these sales weren't sales at all but were consignments.

MR. BICKS: That may or may not be so. We don't have to prove that much. The fact will be made clear through the testimony of the purchasers here, the personnel of the Pension Fund and of Connectibut Mutual, that they specifically addressed questions to all those concerned as to whether these sales were final, whether Topper accepted any returns, and were told flatly "no."

THE COURT: Did they address those questions to First National City Bank?

MR. BICKS: No. The questions that were addressed to First National City Bank will also be the subject

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of testimony and dealt with the questions "Are there any problems with Topper, what does your audit of receivables show." But that will be a subject of testimony and I don't want to characterize it. I think you should hear it directly. What I have done is with regard to each of these practices called your attention to Citibank's knowledge thereof at the time they occurred.

THE COURT: Citibank apparently had knowledge of this question of making --

MR. BICKS: Returns and exchanges.

THE COURT: Returns and exchanges was going on.

MR. WOLLEN: I am sorry. I didn't hear the last couple of words.

THE COURT: I say Citibank apparently had knowledge that this practice of making arrangements with customers where they could return unsold merchandise was going on.

MR. BICKS: That's right, and then the relevance is twofold. It obviously is background to the financial problem that occurred in late 1971.

MR. WOLLEN: There is a lot of evidence in the record as to exactly what that knowledge is and I think the record should reflect that what is going in as part of the plaintiffs' case here is not all of the evidence.

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THE COURT: I assume that.

MR. WOLLEN: Again, I didn't hear the last couple of words of your Honor's sentence.

THE COURT: I said it seems from what little I have heard so far that the Citibank had knowledge that Topper, and apparently other toy manufacturers, as far as I can make out, from what little I have heard about the other part of the industry, that Topper is just a bit more aggressive than the others in the same type of merchandizing.

MR. WOLLEN: You may be talking about two different things, your Honor. There has been some testimony in evidence about returns being made and exchanges being made pursuant to an arrangement made by Topper with the customer prior to the time the sale was made.

THE COURT: Right.

MR. WOLLEN: On the other hand, it's quite a different thing, it strikes me, if a return or an exchange was entered into long after the sale was made as an accommodation to a customer at that time. I don't think there is any evidence whatsoever in the record that Citibank had any knowledge of the former, namely, that agreements were made prior to the time of sale for customers to return merchandise.

That's my specific point with respect to

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Mr. Garvin's testimony, the bottom of that page having been crossed out, because the question was specifically asked of him whether the customer was given that right at the time of the sale. He said not to his knowledge. That illustrates the problem with putting in this testimony which is already in the record in a piecemeal fashion.

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THE COURT: I see. Your point is --

MR.WOLLEN: That toy companies, like all other companies, and maybe more than all other companies, as a matter of accommodation to customers put back merchandise after the sale ~~had~~ has been made and booked, and, of course, Citibank had knowledge of that. I think the plaintiffs had knowledge of that in this case also. The question becomes whether Citibank ~~has~~ had knowledge that sales were being made pursuant to arrangements whereby Topper was obligated to take them back. That is an entirely different thing, and we have not heard any evidence of that.

MR. BICKS: That is not the question right now; plaintiffs' do not believe they are in any way obliged to show that Citibank knew of each of these written agreements. Bear in mind Garvin's testimony is the key on this. It is exactly the bank's knowledge as to what the common industry practice was that the Pension Fund called the bank to get and did get.

THE COURT: What did Garvin say?

MR.BICKS: "It is common in the toy industry; that is what my lending officers told me." I think that is what he said.

MR. WOLLEN: Your Honor, what I was referring to is on page 43, the question following what Mr. Bicks

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read:

"Q Is ityour understanding that such rights are given to customers at the time sales are made?

"A I have never heard that those rights were given to customers."

MR.BICKS: I can read you the quote I have in mind.

THE COURT: Where does it come in?

MR.BICKS: Returns and exchanges.

THE COURT: And we are talking about Garvin?

MR.BICKS: That is right, your Honor.

THE COURT: We are on page 53?

MR.BICKS: Yes, at pages 52/53. That is where he sums it up:

"As I indicated before, I have been told by the lending officers the deal in the toy business that it is common market practice to make sales and at the end of the Christmas season frequently some of that merchandise is returned, and, therefore, you can look at it as a consignment, rather than an outright sale."

That is exactly the knowledge plaintiffs claim Citibank had, and that is the knowledge that they called upon Citibank for.

THE COURT: Mr. Wollen's point is that they didn't

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think they would be obligated.

MR. WOLLEN: Nor is there any evidence of the extent of those returns that Citibank had. The evidence is not complete.

MR.BICKS: On that point, your Honor, I suggest you look at the documents, the Citibank audit reports, which make reference to the volume of reserves for returns they were creating throughout this entire period.

MR.WOLLEN: Just so the record is complete,so do the financial statements of Arthur Young & Company.

THE COURT: All right, we will see you at 2 o'clock.

(Luncheon recess taken.)

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MR. DAILEY: Your Honor, plaintiffs next call Nathan Greenman.

NATHAN GREENMAN, a witness called on behalf of the plaintiffs, being first duly sworn, testified as follows:

THE COURT: I apologize to you, too, Mr. Greenman.

THE WITNESS: That is all right.

MR. DAILEY: Once again plaintiffs would offer into evidence 13 exhibits relating to Greenman Brothers and the Topper Corporation, which will be the subject of Mr. Greenman's testimony this afternoon.

* * * * * * * * * * * * * * * *

DIRECT EXAMINATION

BY MR. DAILEY:

Q Mr. Greenman, what is your present occupation?

A I am executive vice president of Greenman Brothers, wholesale toy distributors.

Q Where is Greenman Brothers located?

A 105 Price Parkway in Famingdale, Long Island.

Q What particular region or regions does Greenman sell?

A Well, we think our trading area consists of a radius of about 300 miles from Metropolitan New York City. We go upstate as far as Buffalo, slightly into Massachusetts, Jersey and Connecticut, and we also have branches.

Q What types of customers does Greenman sell to?

A Independent retail toy stores, mass merchandisers, major department stores.

THE COURT: What is that?

THE WITNESS: Mass merchandisers, such as discount stores, Korvette's and people like that.

Q What is the approximate dollar volume of Greenman's sales? What was it this year?

A Well, for the fiscal year ending January 31 -- I also neglected to say we have branches in Birmingham, Alabama, Miami, Florida, and Washington, D.C. -- and there is a combined total of approximately $70 million.

THE COURT: 70 million?

THE WITNESS: 70 million, yes, sir.

Q Do you recall approximately what your sales were around 1970, 1971?

A Well, I would guess $35, 40 million. It is a guess. We also have a houseware division which does about $15 million, which is incorporated into the figure I gave. So if you took the housewares out, our toy volume would probably be presently about $55 million. I don't recall exactly when we went into the houseware business, about 1970.

Q Is Greenman a public corporation?

A Yes, we are.

Q When did you go public?

A June of 1967.

Q Focusing again on the period '69 through '71, which is relevant to this lawsuit, who were the principal suppliers of toys to Greenman Brothers?

A Well, Mattel, Ideal Toy, Topper, ~~Tonkrite~~ Tonka -- I can probably name you 20 of the largest.

Q Most of the major ones?

A Right.

Q Do you recall what the approximate dollar value of purchases Greenman made from Topper during this period, by year, approximately?

A Well, I would guess at the time you are referring to we did somewhere in the vicinity of a million dollars.

Q About a million dollars a year?

A Well, it worked up to it. I don't know exactly when we started. I can only give you the list of the companies, but as they grew, we grew with them.

Q When did you begin doing business with Topper? Do you recall?

A I don't recall the year, but the original business, they were manufacturing items for supermarkets that they sold through the A&P or food markets, and then they went into the toy business, and as soon as they went into the toy business, manufacturing toys, we were one of the first distributors to carry their products.

Q Were you personally involved in any of the dealings between Topper and Greenman Brothers?

A Yes, sir.

Q I would like to have you explain to us a little something about the pattern of sales in the toy industry? You are a distributor?

A Yes. Incidentally, I must tell you

Greenman Brothers is also involved in some retail sales.

Q You do retail?

A Yes, we have a retail extension of our business, but I don't think it would have any effect.

Q Mr. Greenman, you are in two of the three phases of the toy business, a distributor and retailer of toys?

A Yes.

Q As a distributor of toys when would you order most of the merchandise for sale?

A Somewhere between the 1st of March and the 1st of April we place our orders. Toy Fair is presently on now. I just came down from the Toy Building, and we look at the merchandise, look at the lines. We don't have time to place the orders at the time because Toy Fair only runs ten days. So we pick up our catalogs, make our notations, go back to the office and start writing our orders, between March 1st and April 1st.

THE COURT: Toy Fair is here in the city?

THE WITNESS: Right. It is presently being held in the Toy Building, 200 5th Avenue.

Q What is the most significant part of the toy season at the retail level during the year?

A You mean in sales?

Q Yes, when most of the goods are sold to the ultimate consumer?

A If you pick up the latest Toy Fair edition, Toys and Novelties and Play Things, two separate publications, there is an article in them that is pretty factual, and I believe I read last night that about 75 per cent of the toy business is done in the last quarter of the year.

Q Is that the retail toy business?

A Retail. We are talking about toys, not wading pools or gyms.

Q Do the results of this survey accord roughly with your own experience?

A Pretty much.

Q About 75 percent them is done in October --

A In October, November, December, right.

Q As a distributor what is your most significant season in terms of the months of the year?

A The biggest shipping months we have are September, October, November, and December is substantial with us because we are a local outfit. A good number of the major manufacturers are local, such as Ideal, and we can get a supply from them quickly. So while it is a short month, December generally was almost equal in volume to November, I would say pretty much the same.

Q So as a distributor your significant months are September through December?

A Right.

Q I take it that is the early part of December?

A Yes.

Q That is when you would ship to the retail stores?

A We would start shipping toys in June, July, but a man would come in and buy a dozen, and then he would buy more. If his business picked up in October, November, that is when he would reorder.

Q Was there a relationship during the years '69 through '70 between your ability to ship merchandise and the extent to which the retailers were selling the merchandise?

A I don't understand the question.

Q Well, I believe you testified something to the effect that you would ship them the merchandise when they needed it?

A Yes, sir.

Q I gather, then, that the extent of their shipments would depend upon the demand at retail for the products?

A That is right.

Q When would most of the merchandise be shipped from the toy manufacturer to the distributor?

A Well, it really depends on the products.

Presently you come to a toy manufacturer, he shows you a line. Now, I may start shipping at any time from April on, depending upon the availability of his raw materials. But I would say the line should be complete by July. There are exceptions where an item could be late through some kind of mechanical defect, but the product is completed by July.

Q The heavy shipment season in your experience for a manufacturer would be in the summer?

A No, I can't answer that. We place an order. If we buy 300 dozen, we may ask him to ship a hundred dozen as ready, and then another hundred dozen August 15th, another hundred dozen October 1st. And then from there on we will buy as we sold.

Q I am trying to get some feel to the lead time required of a manufacturer to get his goods into distribution channels in time for the Christmas season. During what months of the year would a toy manufacturer ship a substantial portion of merchandise?

A Well, I can tell you that the peak of our inventory in our warehouse, I think it is heaviest at about October, in October.

Q So that shipments would come some time before October?

A Maximum, and,of course, as our sales go .

If we are selling and receiving in equal amount, we never go higher than that.

Q You testified earlier, I believe, that your best judgment was during the period 1969 through 1971 you did approximately a million dollars or so with Topper?

A Give or take 20 percent.

Q It built up to that? That was the maximum level?

A I would say it is close enough. I could not be sure. I could have found out if I knew you were going to ask the question.

Q During this period again, 1969 through 1971, do you recall if an instance ever arose where Greenman Brothers was unable itself to distribute or to sell to its customers all the Topper merchandise which it previously purchased?

A Yes.

Q On those occasions was there any general practice or pattern of dealing between Greenman Brothers and Topper with regard to the unsold Topper inventory?

A It would depend upon the product and to what extent. Television has played a very important role in the toy business, and sometimes a manufacturer coming into a market, putting on a television ~~camapgin~~ campaign and spending money wants to make sure that there is enough product in the market, and so if you want to buy a hundred or 150 dozen, he may ask you to buy an extra hundred dozen, so that he was sure there was enough in the market, and if worse came to worse, they would exchange it for something else in the line.

Q What does an exchange involve?

A There were two ways you could do it. They would take it back and give you something else you really needed, or if they thought you could dispose of it, they might give you a markdown, an allowance so you could dispose of it at a better price.

Q When they took it back and you say gave you something you really needed, would they actually as your truck came in, would they take the merchandise out and put some more merchandise in and ship it back to you?

A Well, it did not work that way. They would give you an authorization to return it, and if you returned $10,000 worth and they sent you $10,000 worth of a different product, it was to all ~~intends~~ intents and purposes the same thing.

Q You would get a credit of $10,000 against which you would purchase future merchandise?

A Yes.

THE COURT: Is this just with Topper or the toy industry generally?

THE WITNESS: It was not everything we bought from Topper or the toy industry in general. Certain manufacturers, the toy manufacturer, he is the one that makes any money on television toys and he wants to make sure that when a customer walks into a store it is there to be bought. They made the investment. They already bought the TV time and they paid for the commercials, and so they want to make sure that they utilize as many dollars out of this market as they can. But it is not a practice. You can't call it a general practice. But it would depend. Naturally, some of the major toy manufactuerers, like Milton Bradley or ~~OR~~ Tonka that don't make promotional merchandise, they never have that problem. If you want to buy a hundred dozen, you buy a hundred dozen. They know they are not going to have that problem.

Q Did this practice which you have just testified to occur with regard to Topper in 1970?

A Yes.

Q I call your attention, Mr. Greenman, to Plaintiffs' Exhibit 1316, which is the first exhibit in your book, a Topper Corporation memorandum from Alex W. Hughes, Jr. to Sandy Obolsky. I have no reason to believe you received a copy of this memorandum at the time it was written?

A No.

Q I ask you to glance at it. Do you recall the transaction which is reflected in Plaintiffs' Exhibit 1316?

A Pretty much so.

Q Could you tell us what it involved, please?

A It is an agreement that I made with -- I don't know whether I made it with Henry Orenstein or Fred Pierce or somebody.

Q Some officer at Topper?

A Right, in which they would give me a markdown on three of the items, and they went ahead and gave me a thousand pieces of another item at no charge to adjust the inventory. Suppose I had a thousand pieces that cost me $5. Rather than give me $2-1/2 off, if they had enough merchandise they would give me another thousand for nothing, which would have reduced the cost to half.

Q I call your attention to the last sentence in the memorandum, which reads, "Categories not covered in this meeting were: Dawn, Jet Power, Johnny Lightning Cars and Jet Power Cars, new 500's, Ricochet, and Luv 'N Care."

Mr. Greenman, do you recall whether during the course of these discussions you had with some Topper officer ~~and~~ an understanding being reached between Greenman Brothers and Topper that with regard to this merchandise, the Dawn, Jet Power, Johnny Lightning Cars and the others, that you would put off any firm understanding as to what would happen till the end of the ~~years~~ year?

A Yes, that is exactly what it was. We made a definite agreement on the three items above, but the rest would be held in abeyance until it was finally determined.

Q What was the purpose, the reason for holding these in abeyance?

A Well, the memorandum is written July 13th and the items that they give us allowance on, I remember, was some jewelry items which were pretty bad, and the others, I guess they still figure that we would have a good chance of selling, and they said, "Okay, you just try and do what you can with it and at the end we will talk about it later."

Q I call your attention, Mr. Greenman, to Plaintiffs' Exhibit 1317, which is a letter from Greenman Brothers under the name of Alan Chaikin, to Mr. Henry Orenstein of the Topper Corporation, dated October 29, 1970.

Who is Mr. Chaikin?

A He is now our vice president in charge of merchandising. At that time he was the toy buyer who worked for me.

Q During this period how did Mr. Chaikin's responsibilities relate to yours?

A Well, we worked together. We would be in on the conversations and after we established a line, he would do the reordering and handle the details.

Q Were you generally familiar with the various negotiations which Mr. Chaikin was carrying on with manufacturers?

A Very much so.

Q Were you familiar with the negotiations Mr. Chaikin was carrying on with the Topper Corporation?

A Very much so.

Q I call your attention to the second sentence in the first paragraph in the letter, which reads:

"This merchandise per your agreement with Nat Greenman, was to be credited to us at this year's price. Namely, $55.96 per deal and not at $51.94 as your credit calls for."

First, Mr. Greenman, I ask you whether you recall some time around the period when this letter was written, namely, the end of October, 1970, that Greenman returned Johnny Lightning Cars to Topper?

A I am sorry, whether we returned any?

Q Yes.

A Yes, we did.

Q And what were the reasons underlying your returning the merchandise?

A In this particular case, these Johnny Lightning Cars, they were sold to us at $51.94 a deal of 96 cars.

Q Do you recall when they were sold to you?

A I beg your pardon?

Q Do you recall when they were sold?

A Well, it had to be a few months prior to that, with the understanding that they were going up in price. In other words, they come out with a new series for the following season, and they were going up in price, and at the time the new ones were arriving they would take back the old ones and in exchange for new ones.

However, they were going to give us credit for those they took back at the newer price. That was the inducement ~~indicement~~ for us to take advantage of it.

Q I call your attention, sir,to Plaintiffs' Exhibit 846, which is next in your book. This also is a letter from Mr. Chaikin to Mr. Pierce of the Topper Corporation. This letter is dated November 12, 1970.

I call your attention to the first sentence of the second paragraph, which reads:

"Nat Shaffir was out to see me yesterday and we had a discussion concerning merchandise that is beginning to be a problem in the inventory."

And then it goes on focusing on this time period, early November, 1970.

Do you recall Greenman Brothers was having a problem with Topper merchandise in its inventory?

A I guess if you can call it a problem.

Q How would you describe it, sir?

A Well, we had an understanding that -- we did not buy everything on the same basis. There were items that were going to be televised or promoted, and we had an understanding that if there was an excess inventory it would be exchanged for other merchandise.

Q Was this understanding in writing, sir?

A I don't think so.

Q Was it just part of the pattern and practice of dealing between Greenman Brothers and Topper?

A Between myself and Henry Orenstein.

Q Mr. Greenman, during 1970 and 1971 approximately what amount of the Topper line would be considered promotional in the sense which you have been using it this afternoon?

A It's a very difficult question for me to give you an honest answer, you know, a factual answer.

Q Is Johnny Lightning considered to be a promotional item?

A Yes.

Q Was Dawn doll considered to be a promotional item?

A Yes.

Q Those were the two principle lines of Topper toys at the time, were they not?

A No.

Q No? What other lines were there, sir?

A They made major dolls, a large doll.

~~Q~~ Suzie Homemaker was housekeeping, toys. But they made -- their big volume item was the major dolls that they promoted on television, Baby Party.

Q Was Baby Party a promotional item?

A I'm sorry. It might not have been in that year. But they were a very, very important resource for large dolls which cost somewhere in the neighborhood of of about $9 and change. I mean, that was a major category, but they also made other items. We did a lot of business with them and I don't think it would be fair for me to say that Dawn and Johnny Lightning was the major part of it.

Q Perhaps my question was unfair, sir, because I was referring to Topper's own records, not to your own dealings with them.

A OK. I just wanted to tell you what I remembered.

Q But Dawn was a promotional item.

A Yes, very much so.

Q And Johnny Lightning was a promotional item.

A Very much so.

Q And the understandings and arrangements which you have been testifying to applied to Dawn and Johnny Lightning because they were promotional items.

A Right.

Q I call your attention next, Mr. Greenman, to Plaintiffs' Exhibit 1318, which is a letter from Mr. Chaikin of Greenman Brothers to Mr. Shaffir of Topper ~~Corporated~~ Corporation dated November 30, 1970. Who was Mr. Shaffir?

A Nat Schaffir was our Topper salesman. He was the contact between us and the company.

THE COURT: He worked for Topper?

THE WITNESS: He worked for Topper.

Q Did you personally have any negotiations with Mr. Shaffir?

A Really, outside of placing an order with him, but I don't think -- I wouldn't have made any arrangements with Shaffir because I don't think that he would have had the authority to make any arrangement.

Q I call your attention to the first paragraph of the letter, which reads, "I am writing this note to confirm our telephone conversation of November 27 where you agreed to allow us a markdown on the following," and three items of toys --

A Yes.

Q Is that an example of the type of markdown allowance which you described earlier?

A Yes.

Q And this allowance was given in lieu of returning the merchandise for credit?

A Yes.

Q Then you would attempt to sell the merchandise yourself, given this extra markdown?

A Right.

Q Do you recall, Mr. Greenman, whether, as 1970 came to an end, Greenman Brothers was approached by Topper with respect to placing a rather substantial order for Topper merchandise under a program which --

A Yes.

Q -- was commonly referred to as the Spring '71 Program?

A Yes. You mean on an import?

Q Yes. What do you presently recall about that program and what was said to you by Topper with respect to it?

A Well, the Dawn dolls were manufactured in Hong ~~Kong~~ Kong, dolls and clothing, and they sold an import program where you bought it by containers from the Orient and when they came in they came directly to you and for which they effected a savings cost and they passed it along. So instead of the merchandise coming into New York and into their warehouse and transshipping it back to us it came to us directly from -- it was supposed to come to us directly from the pier, which is not an uncommon practice, incidentally. It's being done today with factories except that it's being done on a little different basis. They are buying it now on a letter of credit, paying for it, and this was not done in that case.

Q You say it was not an uncommon practice. Are you referring to the drop shipment from abroad in containers?

A Yes.

Q What was the approximate dollar volume of the merchandise which you purchased under this program?

A A guess would be made a couple of hundred thousand ~~collars~~ dollars. I could be off on that, but --

Q I don't mean to trap you, sir. Obviously it's been some time.

I call your attention to the last exhibit in your book, which is marked Plaintiffs' Exhibit 332, which is a listing of extended dating invoices of Topper Corporated dated December 31, 1970.

As you can see, the Topper customers --

A Yes, I know them.

Q They are there alphabetically. If you could just page through and find Greenman Brothers --

MR. WOLLEN: Mr. Dailey, what number is that?

MR. DAILEY: 332.

Q I believe it's on page 19. The page number is in the upper right-hand corner.

MR. WOLLEN: That is not among the documents that you have offered immediately prior to Mr. Greenman's testimony.

MR. DAILEY: Yes, that was offered as part of

Mr. Bicks' this morning.

MR. WOLLEN: I see.

A I see it. This is --

MR. WOLLEN: I am sorry, but perhaps you could just give us a minute to get that out. That was evidently submitted this morning.

MR. DAILEY: Here.

MR. WOLLEN: Yes, let me take a look at it.

Q Under the account of Greenman Brothers how much merchandise is listed for --

A It shows $286,000. Am I right?

Q Perhaps you are looking at --

A Oh, I am sorry. I beg your pardon. I was looking at this. You mean the end column?

Q Yes, the total column.

A I was looking at this column here.

Q What is the amount --

A I can't see the headings.

That shows $573,000.

Q That is the total?

A Right. But I don't believe all of this ~~cale~~ came through on that import program, container program.

Q According to the invoice, it looks like one half of the total amount is due May-July, and that is

#286,000, and the second half is a dating beyond July, and that is #286,000.

A Yes.

Q Do you recall whether that in fact was the arrangement, that half the merchandise would be due for payment in May and the other half sometime after July?

A I can't recall exactly, but I believe that my arrangements with Henry Orenstein were that -- you know, we put a payment date on it, but it was negotiable at the time it had to be paid for.

Q It was negotiable at the time it had to be paid?

A If we didn't sell the merchandise, it was still in stock, we would extend it.

Q He would extend it for you?

A Yes.

Q So effectively you did not have to pay for the merchandise until you sold it?

A Well, that wouldn't -- I mean, that's what it is, but we wouldn't quibble to that extent.

Q Was that implicit?

A Yes.

Q What if anything was said by you with regard to what might happen with the merchandise which you purchased if you were unable to sell it at the time you placed the order?

A Certain of the items we would make an adjustment on, either exchange, markdown.

Now, I mean, I am not -- you know, we like to feel that we are pretty good toy merchants and we didn't buy it just to buy it. We only bought that which we thought we could sell, with a little bit of coercion to buy a little bit more, but I wouldn't buy #200,000 of goods if I didn't think I could sell it, you know. I figured I might not sell it all, I might sell 75 or 80 percent of it, you know. But I wouldn't have bought it just with the idea of exchanging it.

Q Right. You figured you might be able to sell say 75 percent.

A No, I hoped to sell it all.

Q Right. But if you only sold 75 percent what was your understanding with regard to the 25 percent?

A It would have depended upon the item. I told you. If it was a basic item that would be a continuing item in the line next year and it was current, nothing would happen. If it was an item that was being promoted in that year but would not be promoted the following year, then it could be exchanged.

Q Do you recall having any specific written agreement with Topper with regard to this purchase?

A No.

Q You, in making the order, then simply relied on the pattern and practice of dealings between Greenman Brothers and Topper?

A I am sorry. It might be that when Mr. Chaikin wrote the official purchase order he might have made some notations on it. I don't know. I mean -- but the understanding was an understanding that I had with Henry Orenstein which went over a period of years and I believed Henry Orenstein to be an honorable man and I took his word for it and I never had any problem with it.

THE COURT: Did you have similar arrangements with any other toy manufacturer?

THE WITNESS: I would say maybe on -- not quite the same degree.

Q By degree you mean dollar volume?

A No. Henry just thought that he was -- that he knew how to run your business better than you did, that's all.

Q I call your attention, sir, to Plaintiffs' Exhibit 1319. This is a letter from Greenman Brothers, Mr. Chaikin, to Mr. Shaffir of Topper Corporation, dated

December 3, 1970.

A Right.

Q I would like you to focus on the first sentence, which reads, "As you know, we received on November 25th 1578 dozen of number 700 Dawn outfits that we had not ordered. As we had discussed and you agreed, that on the previous Friday I had not released that merchandise.

"We cannot sell this merchandise prior to Christmas, ~~specially~~ especially when we have substantial amounts of very similar goods coming in on our spring order."

The letter, sir, is dated November 3.

A December 3.

Q Excuse me. December 3. And it indicates that on November 25 you received a large shipment of Dawn outfits. 1578 dozen, I guess, is large.

What was the basis, do you know, of the statement that at this time, in late November, early December, you could not sell the forthcoming Christmas season?

A Well, we said that we had enough of it in stock and we had -- it could have been a mistake or duplicate shipment. It was something that we received and we figured at that point we would not sell that out by

Christmas, and so -- and we had bought a spring promotion for goods to come in after, so that we wanted.

I really did not want to keep things going. If something came in that was wrong and it wasn't there, I figured I would have other things to negotiate at the end, so I wanted to get that out of the way, and so I said, "We didn't buy it, get it back."

Q I call your attention, sir, to Plaintiffs' Exhibit 1320, which is another letter from Mr. Chaikin to Mr. Pierce. This is dated January 6, 1971. The letter recites in the first sentence, "We received today a shipment of Dawn merchandise from your company. In this shipment you overshipped us in the amount of 100 dozen of the number 553 music box and 150 dozen of the 563 six doll case."

A Yes. It was a case that held six Dawn dolls.

Q Yes. Is that instance, sir, in addition to the overshipment of merchandise ~~qhich~~ which apparently occurred in December or were these transactions related?

A No, it had to be different, because it said, "Received today." It's happened -- we have had more than one, two, three, four, five instances where goods were shipped. It could be through an error. Sometimes a factory duplicates an order or whatever. But this was different. The other was dated in December. This is January.

This says "We received today," so we must have gotten it -- it couldn't be the same order.

Q And this was Dawn merchandise?

A Well, 553 was a music box.

Q It was in the Dawn line?

A I believe, yes.

Q It was a music box for the little girl doll --

A Right. No, no, no. It was a music box for a little girl to play with. You have seen these. They open up and they play music.

Q But it was in the Dawn line?

A It might have had a Dawn picture on it, right. I don't remember. But I believe it did, yes.

Q At the time you received this shipment of Dawn merchandise you didn't believe you could sell it yourself?

A Well, Mr. Chaikin said that it was overshipped and he wanted to return it. I happened to have been in the Orient ~~in~~ on January 6, 1971, so I -- I made a trip every year in January for three weeks.

He got it in, it apparently was overshipped, and he just asked ~~for~~ them to return it; he wished to return it.

Q I call your attention, sir, to Plaintiffs' Exhibit 1321, which is another letter from Mr. Chaikin to Mr. Pierce, and this is dated February 3, 1971. The first sentence reads "I am writing this letter to finalize our discussion of last week with respect to the ~~set limit~~ settlement of our 1970 inventory problem. I will point by point list what we discussed so there will be no confusion at any later date."

First I ask, Mr. Greenman, approximately during what period, if there was one, would Greenman take stock of its own inventory and seek to make any arrangements or adjustments with the toy manufacturers?

A There would be two times we would do it. I would try to have done it probably the month before Christmas, so in the event that they decided to give me a markdown, I could dispose of it for the Christmas season; and if that wasn't done, it would be done right after Christmas so I could get it out of my -- you know, out of my place if it wasn't mine.

Q Are the items which are listed in the letter a part of Greenman's 1970 inventory problem as used in this letter?

A Yes.

Q Calling your attention to paragraph 1, which reads "As per your R.A.," which I believe stands for return authorization --

A Right.

Q -- "number, I am returning," and it lists 26,544 pieces of number 700, 1200 pieces of number 553 and 1800 pieces of number 563.

Do you know, sir, what merchandise that was? It's only listed by Topper's invoice number.

A The 26,000 pieces ~~was~~ were Dawn merchandise.

Q And this was a 1970 inventory problem?

A Right.

Q I call your attention, sir, to Paragraph 3, which reads "We are redating the following merchandise as we discussed."

What was involved in the practice of redating, sir, between Greenman Brothers and Topper?

A OK. Incidentally, I negotiated this arrangement.

Q You personally negotiated it?

A I did, right, and Mr. Chaikin was with me; and when they made the arrangement, I came back and I had Mr. Chaikin write Fred Pierce so we would have on record exactly what I had agreed to with Henry Orenstein; and he gave me permission to return the first two items and the third one we are redating, which I said before -- these were Suzy Homemaker, ovens and ice cream makers, which were basic and continuing items in the line, so that instead of taking them back and having to rebuy them maybe, you know, he said "OK, you got them there, we will just redate the invoices as though they were new merchandise."

Q Was there any understanding between Greenman Brothers and Topper with respect to what would happen in the event that the redated merchandise was not sold?

A There was in certain cases. In other words, if --

Q What was that understanding?

A Well, they said "OK, it's going to be in your next -- it's going to be a current item running next year," and so on and so forth, and I said "OK, Henry, as long as it is, but if it isn't I am not letting you off the hook," and at that point I didn't know, but if it was going to be in the continuing line next year; however, if it wasn't, it would have to be renegotiated.

Q At the time --

A At a later date.

Q Is that practice, sir, reflected by the paragraph which begins at the bottom of page 1 and carries over to the top of page 2-F?

A Which reads "We are redating"?

Q Yes.

A Yes. And an item in paragraph 4, you notice they agreed to give us markdowns on some other merchandise, and once they gave us a markdown that was finished, that was not negotiable any longer.

THE COURT: That just became your merchandise at a lower price?

THE WITNESS: Right.

Q Skipping ahead, sir, to Plaintiffs' Exhibit 1322, that is a letter from Mr. Pierce of Topper Corporation to Mr. Chaikin of Greenman Brothers, dated March 24, 1971, relating to a confirmation of redating in the amount of approximately $54,000.

Is this, sir, a confirmation of the prior deal which you testified on just previously?

A I can't answer that honestly because it might have and it might have been something else. It could have been something we had bought either subsequent -- before or subsequently, but it had to do with something that we bought on the condition that if we sold it by a certain date we would pay for it; if not, it would be redated, and apparently we didn't sell it, so they redated it.

Q Next, sir, I call your attention to ~~Plaintiffs'~~ Plaintiffs' Exhibit 1323, which is a letter from Mr. Chaikin to

Mr. Pierce of Topper Corporation, dated May 6, 1971, and which reads in the first paragraph "Pursuant to our past conversation" -- and this is between Chaikin and Pierce, I guess -- "concerning our overstock of merchandise that was shipped to us in December of last year and January of this year, I am listing below the style numbers and quantities that I feel are ~~exceccive~~ excessive and should be moved at once," and then follows two columns which list by invoice number certain --

A By item number, item number and quantity. Is that what you are talking about?

Q Yes.

A Like 500, 12,000 pieces?

Q Right.

A Well, I don't know. If you refer back to it, it might have been something that we accepted a redating on and that -- I don't know. But there is no question that that's part -- it was excessive, something that we felt didn't belong to us.

Q Right.

A Now, I don't know whether it was the same merchandise that was discussed in a prior letter.

Q Right. Can you identify from the invoice, the style numbers there, any of the Topper merchandise which is excessive as of May 6, 1971?

A Very difficult for me to remember. I mean, I am sure it had to do with Dawn, the 500 -- anything we bought 72,000 pieces of was a Dawn outfit, it had to do -- it was an inexpensive Dawn dress, I suppose.

Q Next, sir, I refer you to Plaintiffs' Exhibit 910, which is an internal Topper memorandum, which I do not believe you would have had occasion to see at the time it was written, from Mr. Shaffir to Mr. Hughes. I call your attention to the paragraph at the bottom which reads: "We will ship to Woodbridge warehouse $200,000 of merchandise. Greenman Brothers has the right to exchange any item in that warehouse before shipped to their own warehouse."

Could you amplify for us, sir, on what the transaction was which is alluded to in that sentence?

A I would imagine it was goods that Topper put into a warehouse which was for our account, which they were going to hold, which we were going to draw against.

Q Was there a specified date when you would draw against them or would you draw against them --

A As you needed.

Q Also the top, sir, the first sentence reads, at the top of Plaintiffs' Exhibit 910, "The following has been agreed by Henry Orenstein and Al Chaikin of Greenman Brothers. We are to take back the following," and then there is a list of merchandise. Is that Dawn merchandise which they were to take back, do you know?

A Yes.

Q And the time period is June 23, 1971?

A Yes. Just so I could -- if I may, I want to -- I would like to clarify something, you know. It seems like we are awful damn fools to keep buying and returning.

You keep saying Dawn merchandise, but each one of these things was a different item. They kept coming out with like a new magazine every week, you know. We didn't buy and return the same goods.

Q But the fact that you were returning did indicate that you yourself were unable to sell them.

A Well, we returned a 1970 item and took a 1971. You know, that was our arrangement.

Q Finally, sir, I would like to call your attention to Plaintiffs' Exhibit 1324, which is a letter from Mr. Chaikin to Mr. Hughes, dated July 29, 1971, and unlike the other correspondence which you have testified about, in the upper left-hand corner there is the notation "Registered mail, return receipt requested."

A Right.

Q Would you review the letter, sir?

A Beg your pardon?

Q Could you just --

A I have it, yes.

Q Do you recall under what circumstances this letter was written and for what reason it was sent by registered mail to Topper?

A Yes.

Q Would you explain --

A Mr. Chaikin was probably getting a little bit of a runaround and decided that we weren't -- maybe just an oral agreement wasn't good enough and we were going to put it in form of registered mail to make sure that we were protecting ourselves on our arrangement.

Q Is it true, as indicated in this letter, that you were once more attempting to return Dawn merchandise to Topper?

A Yes, yes.

Q I call your attention, sir, to the last sentence of the second paragraph, which reads -- I will read you the whole paragraph. sir. "With the return of this merchandise we would be in a position to pay the May portion of the Spring Early Buy invoices, which I am sure you recall were payable one half May, one half August.

I obviously cannot pay any of these invoices until the merchandise has been sold, as they were sold to us on guaranteed sale."

Did Topper, sir, with regard to the transaction at issue there, sell the merchandise to you on a guaranteed sale basis?

A Well, that's what it says here, but I could tell you that as far as my arrangements were concerned, you know, it might have been tantamount to a guaranteed sale, but it wasn't sold on that basis, it was sold on the basis that we would not get hurt with it.

Q It was sold on the same basis as the other transactions?

A As everything else, as any other items I had discussed prior. Our relationship with the company was very good. They were becoming a major factor in the business. We were doing a lot of business with them and they were right here in Elizabeth and we had very close connections and we were very happy at the time all this was going on. It didn't appear to be a problem.

Q Right. But the terms of that sale --

MR. WOLLEN: Will you let the witness finish his answer?

Q Excuse me, sir.

A It didn't appear to be -- you know, I wouldn't have bought it had I thought it was a problem. I was, you know, talked into buying a little ~~but~~ bit more than I might have bought, and I did, because I felt I had the assurance that I would not get hurt with it. I think Mr. Chaikin at this point -- it looks to me as though he was a little bit annoyed because he has been trying to reach them and couldn't and wanted to get it back and couldn't and so he wrote a registered letter to cover it and in it he said "guaranteed sale," which maybe he might not have said, but that's what it ammounts to.

Q As far as you were concerned, the terms relating to that transaction were no different than the terms relating to the other dealings you had with Topper?

A Right.

Q Is that true?

A Right.

MR. DAILEY: We have no further questions.

THE COURT: I take it the last sentence in that letter turned out to be unduly optimistic.

THE WITNESS: Why was that? "At our last meeting" --

THE COURT: No, the last sentence.

THE WITNESS: Well, what year did Topper run into

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their difficulties?

MR. DAILEY: 1971.

THE WITNESS: Was it '71? I didn't realize that. Fortunately we didn't -- it was true on our part.

MR. DAILEY: We have no further questions, your Honor.

CROSS-EXAMINATION

BY MR. WOLLEN:

Q Mr. Greenman, do you recall when in 1971 any problems arose with respect to Topper inventory in your position?

A When?

Q Yes, if at all.

A Well, let me say that I believe that we had problems with Topper inventory in 1969, in 1970, as well as '71, except that they were resolved properly in '69 and '70, and so it never came to be a problem.

Q Do you recall when it first if ever came to be a problem unlike those earlier years?

A We were enjoying good business relations and we were doing a lot of business and when something came about we exchanged it and so it never was a problem, except 1971, I guess, when Topper ran into their problems, that's when, you know, we had an idea, and at that point we were trying to protect ourselves.

THE COURT: His question is when did you get this idea that you needed to protect yourself, the year, as far as you know.

THE WITNESS: Honestly, I can't tell you exactly. I don't know. You know, the toy business is a relatively close business and you hear all kinds of rumors and all kinds of stories and I guess at that point we might have had an idea that Topper might be running into difficulty, so that we were trying to do whatever we could possibly do and protect ourselves.

THE COURT: You can't pinpoint the month?

THE WITNESS: I really can't. When we buy goods at Toy Fair now and I buy it for Christmas selling, I really can't tell you that it's a problem until maybe October or November. It can't be a problem, you know, if it's a basic item, it can't be a problem in June or July, because I did buy it for Christmas selling.

Q As you testified before, that is because the highest point in your inventory is in October, is that right?

A I am sorry, I didn't get you.

Q I thought you had testified before that the highest point in your inventory during the course of any given year was in October.

A Yes.

Q So you really can't tell until October --

A No, no.

MR. DAILEY: I object to that.

MR. WOLLEN: I haven't finished the question.

A You know, some of these were problems from a prior year.

Q No, my question is focused on different problems from those of a prior year.

As you say, you can't specify exactly when in 1971 you became aware that that was a problem.

A All I can tell you is that there is nothing that I bought at Toy Fair in 1971 that I would have considered a problem in May of 1971.

Q Mr. Greenman, in connection with Topper did you ever have any contact with First National City Bank?

A No, I don't believe so.

Q To the best of your recollection.

A No.

Q Did you mention before that Greenman Brothers is on a January 31 fiscal year?

A Yes.

Q Could you explain for me and for the Court why you are on a January 31 fiscal year instead of a calendar fiscal year?

A I think that it's not a difficult -- I think a lot of people -- the major part of toy companies do run their fiscal year to January 31 because of adjustments that are necessary in January, after Christmas.

THE COURT: You would never get your books settled if you had the Christmas rush --

THE WITNESS: What happens is everybody closes up for ten days, you know, and you have got problems.

Q I also think you mentioned that you went to the Orient every January.

A Yes, I used to go -- for a period of sixteen, seventeen years I made the trip once, maybe twice a year.

Q But you also made it each year in January specifically as opposed to some other time?

A I used to make it in January for the first three weeks in January, came back in time for Toy Fair.

Q Can you tell me why you would go to the Orient in January?

A Well, we bought toys for the following Christmas.

Q Was this also, like the January 31 fiscal year, a practice in the industry, people would go to the Orient --

A Yes. Most of the toy makers -- in fact, I didn't tell you, but I used to go from Hong Kong to Nuremburg and make the Nuremburg fair and you met all of the American toy buyers, from Sears Roebuck, J. C. Penney. That's the time they go.

Q In January --

A They go in January to buy goods for the following Christmas. It arrives in the states sometime in August ~~of~~ OR so, August, September, and you have it in time for Christmas selling.

MR. WOLLEN: I have no further questions, your Honor.

THE COURT: Thank you.

(Witness excused)

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February 19, 1976 - 10:30 a.m.

THE COURT: You may proceed.

MR. BICKS: Your Honor, plaintiffs call as their next witness Mr. Henry L. Thompson.

THE COURT: Mr.. Thompson had the conversation.

MR. BICKS: Yes.

HENRY L. THOMPSON, called on behalf of the plaintiffs, having been first duly sworn, testified as follows:

MR. BICKS: If your Honor please, I would like to introduce into evidence the various documents that Mr. Thompson will testify about.

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DIRECT EXAMINATION

BY MR. BICKS:

Q Mr. Thompson, will you please summarize your education and background?

A I was graduated with a Bachelor of Arts degree from Brown University in 1957. I then went to Harvard Business School and obtained a Master of Business Administration degree in 1959. Thereafter, I believe about 1966 or '67, I became a chartered financial analyst.

Q What is a chartered financial analyst?

A Well, to become one you have to be a member of the New York Society of Security Analysts, or a similar body, and then you take a series of three written examinations that are given once each year that would relate to economic security analysis of portfolio management.

Q I believe you said you graduated Harvard Business

School in 1959.

A That is correct.

Q What was your first employment following graduation?

A I went to work for an institutional brokerage firm named H. C. Wainwright & Company.

Q Where is H. C. Wainwright located?

A They are located in New York City.

Q Could you describe your responsibilities with H. C. Wainwright?

A I was a security analyst doing work for institutional clients, which includes banks, insurance companies, pension funds.

Q Could you be a bit more specific as to what you mean by doing work for institutional accounts?

A Well, I would read the financial reports of these companies and then I would go out and interview the managements of them, sometimes in person, sometimes by telephone, and then I would normally prepare a written report which would either be distributed to one specific client or to all of the firm's institutional accounts.

Q About how many years did you remain in this position with H. C. Wainwright?

A Approximately seven years.

Q That would be from 1959 to 1966?

A That is right.

Q What was your employment next following your position at H. C. Wainwright?

A I went from H. C. Wainwright to the Federal Insurance Company, where I became an assistant portfolio manager, and in that capacity I made recommendations on stock and bond securities that were in the Federal Insurance portfolio.

Q And who owned Federal Insurance at the time you were employed by them?

A Federal Insurance Company, I believe, was originally part of Chubb & Son, which in turn became Chubb Corporation.

Q How many years did you hold the position of portfolio manager at Federal Insurance?

A About three years.

Q 1966 to 1969?

A Until April ~~fo~~ of 1969.

Q In April of 1969 what became your employment?

A I then joined the U.S. Steel and Carnegie Pension Fund as an investment manager.

Q And who hired you to come to work at the Pension Fund?

A Harvey Mole, who was then president of the Pension Fund.

Q Did he interview you prior to your going on board there?

A Yes, he did.

Q Did he seek you out or did you apply for a job there?

A He sought me out through Mr. Van ~~Dusen~~ Deusen, who was one of the senior investment people there.

Q I think you said your responsibilities were that of an investment manager at the Pension Fund?

A Yes, that is correct.

Q Could you describe what the function of an investment manager at the Pension Fund was?

A An investment manager would report directly to Mr. Mole. He would have an assigned group of industries which he would be responsible for both the public and private financings in. He would also do any sale/leaseback that would be connected with it.

In this capacity we would quite often interview managements of companies, write memoranda, which would be reviewed by Mr. Mole and discussed with him. In the case of public vehicles we would quite often rely on people in what we consider to be the good institutional brokerage firms.

Q Let us stop just a moment and detail, if you will, how you reported to Mr. Mole. Was it via memoranda or in person, for example?

A Normally when I would see a company, as soon as I returned from the visit I would dictate a memorandum that would be about twopages in length. I would then give that to Mr. Mole and follow it up with a discussion in person. It was a very small organization, so we were in frequent contact with one another.

Q Right. Let's focus for a minute on what I think you indcated was an industry area of responsibility. Were one or more industries assigned to you as an investment manager to follow?

A Yes, they were.

Q What were those industries say during the period 1969 through 1971?

A The industries that we had the most money invested in that I followed would be the drug industry, including the retail trade industry and the non-ferrous metals group.

Now, in addition there were a number of other industries ~~industires~~ that I spent much less time on that we would have one or two or no investments in, such as cosmetics, where we had just one investment in Gillette, textiles, where we had one investment in Burlington Industries. It also might include companies which Mr. Mole specifically would assign to me that didn't fall into any clear-cut bailiwick.

Q You indicated your position was entitled Investment Manager. During the period '69 to '71 how many professionals at the Fund were employed to perform comparable functions of investment analysis?

A There would be approximately ten, including Mr. Mole and going down to the most junior employee.

Q Could you sketch very briefly that structure, just so that the record indicates how many people there were on each level, approximately?

A Well, in the summer of 1971 there would have been

Mr. Mole as ~~present~~ president of the Fund. There were two vice presidents beneath him, Mr. Harrison and Mr. Van ~~Dusen~~ Deusen, I was an investment manager, and to the best of my knowledge, I was the only investment manager at the Fund.

Q That was the level right below the two vice presidents, was it?

A That is correct. And then there were a number of security analysts. I can't be precise about the number because some were hired during this interval, but the total came up to approximately ten, including the four of us that I have just referred to.

Q Right. Apart from Mr. Mole and the two vice presidents, did the various analysts below them, which were six or seven in number, have particular industry areas assigned to each of them?

A Yes, that is correct.

Q Have you completed a listing of the industry areas that were within your area of primary responsibility?

A This would be a very general area that would include about 95 to 99 percent of the money, but I would perhaps have some responsibility in conglomerates or in private placement~~s~~ vehicles that didn't fall into any particular area.

Q As to the industries and companies within your area of responsibility, I think you said that your responsibility was to focus on developments and make recommendations as to the purchase or sale of securities?

A Yes, that is correct.

Q Just follow the progress generally of the companies in which you had investments in addition to that, did you?

A That would be correct. We were both following the companies in which we had funds invested and we were also trying to discover other companies where we could make new investments that weren't currently in the portfolio.

Q Could you sketch very briefly what the process was within the Fund for consideration of a proposed investment or sale in securities?

A Well, after I or someone like me had done the investigatory work and usually written a memoranda, memorandum, we would discuss it with Mr. Mole. He would then in turn give us his ideas, where we should do further work or check out any specific areas that he would want us to look into.

After that we would discuss it again and if he thought it was an investment that was suited to the Fund he would approve the writing of a decision memo, which in turn would go to the Committee on Finance for approval or rejection.

Q Did this process for investigation or consideration of a proposed investment differ at all, on the one hand, when the investment involved a public offering from, on the other, when the investment involved a private placement?

A Well, in the private placement area we tended I think to rely on others outside of the company where we thought they would have particular expertise. In general, if we --

Q Why would that be so? Why would you do that to a greater extent in private placements than public offerings?

A Well, these were less liquid investments and if we went into one of them we do not have the ability generally to free ourselves from it if we changed our mind as easily as if we bought shares in duPont or General Electic or some other company.

Q Go on. You were explaining how the procedure for investigation or consideration of an investment differed in the case of a private placement.

A It would differ primarily in that we would like for someone, such as an investment banking firm that had a record of success in this area and a history of being experienced in it, we would certainly be interested in a bank that could provide us with current financial information on the company which would give us a feel of the condition of it at the time at which we were going to invest, if we felt that we had access and could rely on that information. We also from time to time would make trade checks. This would be the kind of thing.

THE COURT: What is a trade check?

THE WITNESS: This would be with someone in the same industry, your Honor.

THE COURT: A competitor?

THE WITNESS: Yes, your Honor.

Q Or a customer?

A Or a customer, yes.

Q Did there come a time after you commenced employment at the Pension Fund in April of 1969 when you became aware of a relationship between the Pension Fund and Citibank?

A Yes.

Q Could you describe the circumstances under which you first became aware of that relation?

A There were two circumstances. One, there were a series of investment meetings between the ~~very~~ various people at Citibank and the Pension Fund. Memoranda were made of these meetings and circulated to those not in attendance.

In addition, Citibank, through a Mr. Miller --

Q Who was Mr. Miller?

A Well, Mr. Miller was the liaison between the bank and the Pension Fund and the man who arranged these investment meetings and I believe he was the fellow that had the job before Mr. Jeffers took over from him.

Q I just wanted to straighten that out. When did Jeffers succeed Miller, do you know, as the liaison between the bank and the Fund?

A I really don't know.

Q Go on with your first contact with Miller.

A Well, Miller arranged a meeting at the bank's headquarters to discuss a proposed private placement in a company called Beverly Enterprises.

Q How did this come to your attention?

A He contacted George Nelson, who had been -- who was a vice president in 1969 of the Pension Fund before he retired, and invited him to lunch at the bank's offices; and Mr. Nelson, in order to expose me to this relationship, included me as a new employee in on the luncheon.

Q This was soon after you came on board the Pension Fund?

A Within a very few months.

Q What happened at that luncheon?

A Well, we listened to the management discuss its prospects and we decided that we didn't want to do the financing with them after the luncheon.

THE COURT: Management of the prospective investee was invited to this luncheon?

THE WITNESS:Yes, the president of the company and the financial vice president were both there.

Q Who arranged the lunch?

A I believe it was Mr. Miller.

Q What did Mr. Miller say either to you or to Mr. Nelson in your presence in the course of that lunch?

A I don't believe that he clarified the relationship between Beverly and the bank, but he was interested in where we would want to do a mezzanine private placement with the company, since he was familiar with our operation and knew that this was --

THE COURT: What kind, mezzanine?

THE WITNESS: Mezzanine.

THE COURT: What is that?

THE WITNESS: It is a layer of financing that comes after the senior creditors but above the common stock equity. Sometimes it is referred to as sandwich money, your Honor.

THE COURT: Is it like preferred stock or debentures, unsecured debentures.

THE WITNESS: It would, in our case, I believe, always be a debt instrument and it would be convertible to debentures or a note with warrants.

MR.BICKS: Like the Topper notes,your Honor.

(Continued on the next page.)

Q You were indicating Mr. Miller's role in connection with Beverly.

A Well, Mr. Miller arranged the meeting and really chaired the lunchroom. He brought us together, would be his role as I would characterize it.

Q Following that luncheon did you indicate that the Pension Fund concluded not to participate in the private placement?

A That is correct.

Q What was the basis of that judgment, if you know?

A We felt that Beverly Enterprises would not want just one financing, but that they would continually be coming back into the market for additional moneys, and, as a second point, Mr. Christensen, who is the president, I don't believe had any experience in running a large-scale business organization.

Q Did you gain any knowledge in the course of that luncheon as to whether Citibank at the time of the luncheon was lending money to Beverly?

A No, I did not.

Q Have you finished your responses to the circumstances under which you became aware of the relation of Citibank and the Pension Fund?

A Yes.

Q Did Mr. ~~M~~Nelson when he took you to the luncheon describe in any way his view of that relationship?

A I honestly don't remember.

THE COURT: You are not aware of the writing?

THE WITNESS: Not until after the ~~proper~~ Topper private placement.

Q Apart from your knowledge of that particular piece of paper, could you tell us when you became aware of the nature of the relationship with Citibank and the Pension Fund?

MR. WOLLEN: I thought that was asked and answered.

THE COURT: Before you knew about that piece of paper what would you have said about the relationship?

THE WITNESS: It was a very close relationship, in that they performed both custody service and they had investment services which related primarily to meetings between the staff of the Pension Fund and Citibank, but also included going to them on a private placement where we thought they had a particular area of expertise and could be helpful to us.

Q Were you aware that the Pension Fund was paying the Citibank any money for these services?

A I am not sure "aware" is the right word, but I thought they were.

THE COURT: You assumed they must have been? Is that it?

THE WITNESS: I assumed they were not doing it for nothing.

Q Did there come a time in the summer of 1971 when you came to consider a private placement of Topper notes?

A Yes.

Q How was that proposed investment brought to your attention?

A Through Hayden Stone. One of their representatives contacted us and, in turn, led to my receiving a Private Placement Memorandum of the Topper convertible debenture financing.

MR. BICKS: That Private Placement Memorandum to which Mr. Thompson has just referred is in your volume.

THE COURT: What number is it? Don't bother. I don't need it now.

MR. BICKS: It is in your volume number 1 right behind the second yellow tab, sir.

Q You said that Mr. Inglis, of Hayden Stone, called you and sent you a copy of the Private Placement

Memorandum? Is that what you say?

A Mr. Inglis was a vice president of Hayden Stone. He did contact me and he was the one responsible for sending me the Private Placement Memorandum.

Q Mr. Thompson, if I may I would like to hand you a copy of the various documents that have been introduced in evidence. Do you have before you a copy of the Private Placement Memorandum you received?

A Yes. There is a copy, I believe it is marked Connecticut Mutual's copy.

Q A copy of the memorandum you received?

A Yes.

THE COURT: The same thing that was sent to them was sent to you?

THE WITNESS: Yes, your Honor.

Q Following your receipt of the Private Placement Memorandum what did you do?

A I read it.

Q Could you summarize what stood out in your mind when you read the memorandum?

A There were really three things: First, Topper had gone into a program of selling Dawn dolls, which they said would cut down on the seasonal fluctuations in the toy business, and they said that this Dawn line, which I believe was introduced early in 1970, would provide stability to the company.

In addition, I believe in March of 1971 they had become associated with Sesame Street, and they felt that this would be a stable item in the educational sector of the toy market that would broaden their market base and which had good prospects for growth.

In addition, there was a series of projections in the exhibits of the Private Placement Memorandum which presented the company at the end of 1971 as being in good financial position. Specifically, I think they were going to make about $5 million pre-tax, and there was one exhibit in there that showed that the cash inflow into the company was going to exceed the cash outflow by about $27-plus million, and the short-term borrowings were going to be repaid, and, in effect, the company was going to have about five million dollars of surplus cash which they could invest in government securities or whatever they chose to.

Q You were referring to the projections which showed a certain amount of money to be left over in the company treasury at the end of 1971. Was there also included a financial statement~~s~~ or statements as to the company's operations in prior years?

A Yes.

Q What did those show?

A These showed substantial losses in prior years.

Q Which years were those?

A I believe 1967, 1968, 1969.

Q Why don't you take a look at the Prospectus in front of you. I believe they are on pages 6 and 7.

A Yes.

Q What did the company report as income from continuing operations in 1968?

A Looks to me like it is $506,000.

Q Income from continuing operations in '68? Page 6?

A I'm sorry. It looks like --

Q The question is, what was the income from continuing operations before provisions for federal taxes, federal income taxes in 1968?

THE COURT: If you want it in the record, you can put it in.

THE WITNESS: I see a loss figure for the eleven months of $582,000, and then I see a profit of $506,000 for the year ended December 31, 1968.

Q What was the profit figure shown for continuing operations for the year ended December 31, 1969?

THE COURT: Read it into the record. You are not testing his eyesight.

Q Go on and tell us what your thought was after you looked at the income statements back in August of 1971.

A Well, my thought was that the company in the past had a period of substantial losses, but the income as portrayed in that Private Placement Memorandum indicated that if you excluded operations that the company had discontinued, that the toy business was increasing their profitability.

Q Go ahead. You were summarizing your thoughts after you read the memo and referred to Sesame Street and the financial statements. Did you have any other reaction when you read the memo?

A No, those were pretty much the three main points that I considered important in the Private Placement Memoranda.

Q What did you do after you read the Private Placement Memoranda in connection with the proposed Topper investment?

A I met with the management of Topper at its headquarters on August 4.

Q Can you tell us in essence what happened during the day of August 4? Who you met with? What was said to you?

A Well, I met primarily with Mr. Orenstein, who was the president of the company, and Mr. Rose, who was the chief financial officer, and a large part of these discussions took place in the presence of Mr. Inglis.

Q Mr. Inglis arranged the meeting for you?

A Yes, he had.

Q Mr. Inglis was from Hayden Stone?

A That is correct. The discussions that I had on August 4 seemed to confirm that the Dawn line was doing well and the company, I believe, actually was re-ordering additional merchandise to replace the Dawn products that had gone into the hands of children.

Q Who told you that?

A Mr. Orenstein had told me that, and I believe Mr. Inglis had confirmed this earlier in the day.

The second thing that was really discussed was the fact that the company no longer had problems related to consignment; this was discussed in the context with Mr. Rose as to whether sales were final.

Q Why did you bring that subject up? Or did he bring it up?

A Well, I brought it up, and I brought it up because there was a reference in the prospectus to a past period when the company had returns, I believe, something over $4 million due to a bill and hold program.

Q When was that program as referred to in the Private Placement Memorandum?

A I think it was about 1968, but I would have to check that.

Q Why don't you check that and see.

THE COURT: You must know. Tell him.

Q Was the period 1965, Mr. Thompson, 1966?

A There was another reference to it, where the company had sent groups out to supermarkets, I believe, after the Christmas selling season, and that these had been returned, and that this resulted in substantial loss. So that there were really these two references.

Q And it was in light of those references in the past, was it, that you raised this point?

A Right.

Q And just how did you raise it? Will you tell us that?

A Well, I had been in Mr. Rose's office discussing in detail, but not looking at the specific documents, the kind of controls that the company had to, in effect, prevent a recurrence of these past problems. In the course of that he made mention of the fact that they had ageings of receivables; and that there were cash flow projections; and that they had reports which would indicate that they had enough of a lead part to produce a particular toy, but were not overstocked on the standard parts that went into it; and I believe he also made mention that his people worked very closely with Citibank and that Citibank was receiving this kind of information, or, at least, the information that related to collections and ageings of receivables.

We were just getting to the point where I was going to look at these documents, and he said, "Mr. Orenstein is going to have lunch with you in a few minutes. Let us go down and actually see the documents produced at the end of the hall in the computer room."

Then we went down there and I saw the IBM machinery.

Then coming back down the hall I asked Mr. Rose in the presence of Mr. Inglis, "You know, are your sales final?" And he said, "Yes, they are." And then I said, "You know, what about returns?" And Mr. Rose said, "Well, we are very hard-nosed about returns."

THE COURT: What documents were you going to see when he suggested you have dinner instead?

THE WITNESS: His point was that the president of the company was going to take me out of Rose's office very soon to have lunch with the president and that he wanted me to go down and see the product[illegible] these documents, but he was not specific as to what exactly we were going to see. His office was stacked with computer runouts of documents, and he had a great deal of pride in having put in this IBM computer system. I think it was really kind of pride of authorship of having done this, to get away from a period when the company had not been able to coordinate shipments with billing invoices, and he really wanted me to see the documents being produced before we discussed them.

THE COURT: Did he ever show you a contract with one of the distributors?

THE WITNESS: No, your Honor, he never did.

THE COURT: Did you ask him for one? Would that have been crucial?

THE WITNESS: I did not ask him for one. I phrased my question really to him as a general question about sales being final, and then what the return policy was, and he said they were hard-nosed and discouraged them. Then I followed up and said, "Don't you ever do it basically?" And he said, "Well, sometimes we will balance one good selling toy with another." And then I said, "Well, what about one that is not selling well?" And he said, "Well, we definitely don't take back the ones that are not selling and we discourage this."

And then I followed up by asking him what the company's bad debts were likely to be from the accounts they were dealing with, and he indicated they would be simply under $200,000, and probably about $150,000.

I asked him specifically about a couple of the larger chains and his relationship with them, but I did not ask him about any toy distributors.

Q Following this pre-luncheon with Mr. Rose, what happened next?

A Well, I spent some time on the 4th in the presence of Henry Orenstein and, in fact, had lunch with him on the 4th, and it was in the context of this discussion, I believe, that he assured me that the toy business had more stability in the past and the Dawn program was a successful progra and that is how we got into the discussion of Dawn. Then I later took a tour of the various parts of the headquarters and plants and met with various people in the Topper organization.

After that I actually went and saw some of the goods being produced in the plant, and came back, and Mr. Orenstein invited me to go see a screening.

Q Where did all this take place? In the Topper facility in New Jersey?

A In Elizabeth, New Jersey.

Q Who took you back?

A I came back with Mr. Orenstein in his car, I believe Mr. Inglis and a man named Jack Jones, who was an officer of Topper.

Q Was anything discussed on the trip back?

A . Well, on the trip back I asked Mr. Orenstein about this relationship with the banks and he indicated that First National City Bank was the company's banker. And I asked him who the particular individual there was who was responsible for the account, and he told me that Edward Waldman was the senior man on the account. I then asked him if I was free to talk to Mr. Waldman and to get information about Topper's financial condition, and he told me that I was free to do this.

Now, in addition, we discussed a number of other things, which would include the fact that I was probably going to make trade checks of who in Wall Street followed the toy stocks. But that, I think, would be the most important point.

Q When you say that would be the most important point, what were you referring to, Mr. Thompson?

A Well, of the things discussed coming back in the car, that he had given me both the name of a person at First National City Bank where there was this relationship that I mentioned before, that I could check out the financial condition of the company, and had given me the green light to go to the bank if I so chose.

Q I think you are testifying as to what occurred on the ride back from Elizabeth to New York. What happened when you got back to New York?

A In New York it was late in the day and we viewed commercials, I believe, Smartypants and Ding-a-Ling, and that really concluded the day. I went home that evening and made some handwritten notes on the day's trip.

Q Mr. Thompson, in front of you is a document admitted in evidence as Plaintiffs' Exhibit 1371. Are those the handwritten notes you made the night of August 4?

A Yes.

THE COURT: Where would I find them?

MR. BICKS: I believe it is in your book, sir, as the first document, the small book.

Q You made these notes at home the night of August 4th?

A Yes.

Q When you arrived at the office the next day, August 5th, did you dictate a memorandum on your visit of the prior day?

A Yes, I did.

Q Is the document introduced in evidence as Plaintiffs' Exhibit 1372 the memorandum you dictated on August 5, 1971?

A Yes.

Q Is that a memorandum to Mr. Mole?

A It is.

Q Did you deliver the memorandum to Mr. Mole?

A I did, some time on the 5th or the 6th.

Q Do you happen to remember was 5th or 6th towards the end of the week or the beginning of the week in 1971?

A The 5th would have been a Thursday and the 6th would have been a Friday. I remember because Mr. Mole was leaving on vacation on that Friday and was going to be out of the office I believe until the 23rd.

Q Mr. Mole was leaving from Friday the 6th to Monday the 23rd?

A Yes.

Q Did you get to see him before he left?

A I did.

Q Will you tell us what the substance of your discussion was after you delivered the memorandum to Mr. Mole on August 5th or 6th?

MR. WOLLEN: Your Honor, I don't want to be hypertechnical, but don't you think we ought to inquire as to what was said by whom rather than just the substance of the conversation?

MR. BICKS: All right. I can take it in as much detail as you would like.

THE COURT: Mr. Bicks, I just skimmed through this memorandum of August 5th and I don't see First National City Bank mentioned. Have I missed something?

MR. BICKS: No, it is not. I think Mr. Thompson testified that he was told about the bank --

THE COURT: I just thought he put less importance on it at the time than he now puts on it.

MR.BICKS: It is a good point.

MR. WOLLEN: The answer is you didn't miss anything?

MR. BICKS: I think we ought to explore just exactly what importance he did put on it. That's the purpose of the examination.

THE COURT: Yes.

Q Go ahead, Mr. Thompson.

A As I understood your question, it was within reference to this car ride back from, you know, Elizabeth, New Jersey, rather than what happened throughout the full day.

Q Right, it was. Could you state what you said to Mr. Mole and what he said to you on the 5th or 6th following his receipt of your memorandum dated August 5th?

A I couldn't tell you who said what to whom on that, but I can give you an idea of the --

Q Can you state the substance of the conversation then?

A Well, Mr. Mole was going on vacation and I wanted to find out from Mr. Mole whether he would approve doing further work on Topper in his absence or whether he wanted to basically kill the deal right there and I believe we discussed the memoranda -- memorandum and the points that came out were that the Dawn and the Sesame Street line seemed to be giving more stability and that the company had a good set of financial controls and Mr. Mole -- I told him about the Citibank receiving this information and this was a plus, but we didn't really discuss that in any detail at that time, and I believe that Mr. Mole -- I had given him the offering brochure, Private Placement Memorandum, and he in effect said that while he was away that I should check with Glover Johnson and I guess he had a specific question there --

THE COURT: Remind me who is Glover Johnson.

THE WITNESS: He is an outside director of Topper who was a partner of White & Case and I believe -- in fact, I know he is deceased.

A And he approved making trade checks in his absence and he also wanted to get the annual report of Topper for 1970, which wasn't included in this memorandum, and any interim financial statements that had come out.

So in effect he gave me a hunting license to do further work on Topper in his absence and in the memo, in order to be sure that he would get back to me at the end of the week, I wanted to call it to his attention, so that I made the concluding remark a good deal stronger than I intended it in there, and we certainly discussed that and he in effect said "Thomspon, we have some special relationships here that you can check out and then let us talk about it when I get back from vacation."

Q So this was Thursday or Friday, August 5th or 6th, and Mr. Mole went away from Friday the 6th to Monday the 23rd of August, right?

A Right.

Q Let us focus on the period of his absence and what you did during that period. Let us begin the week of August 9th, Monday the 9th.

Do you remember what, if anything, you did on Topper that week?

A At some point early in the week I asked that Mr. Rose come in and actually sit down and show us his financial control system or do more than just discuss it in general in his offices there. The other thing that -- I believe earlier in the week I had a telephone conversation with Christopher Cerf, who was head of the non-broadcast area of Childrens Television Workship, which related to the Sesame Street Product line.

Q You have before you a document introduced in evidence as Plaintiffs' Exhibit 1374. Is that a memorandum of your telephone conversation with Mr. Cerf?

A Yes, it is.

Q You have mentioned in addition to Mr. Cerf that you arranged for Mr. Rose to come in that week?

A Later in the week.

Q Right. Did Mr. Rose come in later in the week?

A Yes, he did. He came in on Friday of that week.

Q What date was that?

A I believe it was the 13th.

Q Tell us what happened before Rose came in on Friday the 13th, if you will, what else you did.

A Well, I talked to Christopher Cerf, who indicated that the Sesame Street line would have an expectancy of five or six years at least and he confirmed the relationship with Topper whereby if Topper developed a specific toy and Sesame Street approved it, Topper had an exclusive on it; or if Sesame Street asked Topper to make a particular toy, they also had an exclusive on it. He actually used the word "thrilled" with the relationship between Topper and the Childrens Television Workship and seemed to confirm what I had been told and read in the Private Placement Memo about Sesame Street adding a dimension of stability to the company's business.

Q Beyond your conversation with Mr. Cerf, did you make any what you earlier referred to as trade checks that week?

A Yes, I did. I believe on probably Monday of the week I phoned people at Zayre and J.C. Penney whom I knew and asked if they would have their toy buyers talk to me and they called up later in the week.

Q What did the toy buyer from J.C. Penney tell you, if you remember?

A The toy buyer from J.C. Penney, No. 1, said that Topper management was honest and I believe said they were hard working. He also felt, I guess in contrast to the toy buyer from Zayre, that they had --

THE COURT: In contrast? I couldn't get that.

A -- to the toy buyer from Zyre, who I actually talked to,I believe, a day earlier or earlier on that day, that they had a competent middle management. He criticized the company for spending a high percentage of its revenues on television advertising, and this was a point I had also discussed on the 4th, I believe, with Mr. Orenstein and which I then took up at the meeting a day or so later with the representatives from Topper.

He indicated to me that this Dawn program was a success and gave the company high marks for being able to introduce it in the face of Barbie, which was the principal competitor of the Dawn line, and he agreed that the outlook for the Sesame Street line was good.

MR.WOLLEN: I am sorry, your Honor. Is the record clear with whom Mr. Thompson is speaking now?

THE COURT: This is the Penney fellow.

MR. BICKS: Yes.

THE WITNESS: I believe his name is Mr. Folan.

THE COURT: I was correct when I said you were talking about your conversation with the Penney man, Folan.

THE WITNESS: Yes.

Q Mr. Thompson, you have before you a document introduced as Plaintiffs' Exhibit 1376. Is that a memorandum of the conversation you dictated shortly after your conversation with Mr. Folan from J.C. Penney?

A Yes.

THE COURT: Did you ask Mr. Folan anything about Topper's return policies?

THE WITNESS: No, I did not.

Q You mentioned, I think, that shortly before your telephone conversation with Mr. Folan you had spoken with the toy buyer from Zayre?

A That is right. His name was Hessdorf.

Q Is Plaintiffs' Exhibit 1375 introduced in evidence and before you a memorandum you dictated shortly after your telephone conversation with Mr. Hessorf of Zayre?

A It is.

Q Can you tell us in substance what you learned from Mr. Hessdorf?

A Well, Mr. Hessdorf felt that Mr. Orenstein was very important to the marketing side of the business and that the marketing personnel beneath him were thin, but he felt that the company deserved credit for its Dawn program and that this was successful.

He also indiated that the trade was looking for a strong No. 2 company to Mattel and I believe cited an instance where Mattel had loaded the trade up with Hot Wheels.

THE COURT: With what?

THE WITNESS: Hot Wheels.

THE COURT: Hot Wheels?

THE WITNESS: Yes. I think it is a racing car line that competed with Johnny Lightning.

THE COURT: I see.

A And that the trade was angry with Mattel because Mattel had said they would make it up to them and the trade hadn't really been willing to take this merchandise, but in effect Mattel did not make it up to them and they were -- it was characterized as let's say laying in wait for them and in effect very willing to do business with

Topper and looking for a strong No. 2 company.

THE COURT: What do you mean by make it up to them? What did they mean rather.

THE WITNESS: Well, I believe that they would give them, you know, first crack at a good line of merchandise if they came in.

You know, I was left with the impression that this was a plus for Topper and it in effect confirmed a statement that Mr. Orenstein had made to me on the 4th.

I asked Mr. Hessdorf about whether the management of the company was honest and he felt that they were honest.

I also asked him about a point that had come up in a conversation with a Mr. Schwartz, who was a toy analyst at Burnham & Company, and Mr. Schwartz had criticized Topper's product line as being shorter than that of Mattel. In other words, if they put out a truck or a doll on the market its life span as an economic entity would be shorter than for a comparable item of Mattel.

Mr. Hessdorf took issue with this. He said if anything it was just the opposite, that Topper could go longer into the selling season than anyone else in the trade. He in effect cut down on the credibility of Mr. Schwartz' knowledge of the toy business.

So that the principal plus I got out of this conversation was that the Dawn program was successful and the trade was looking for a good No. 2 company. The principal negative that came out of it was the fact that Henry Orenstein seemed to be dominating the marketing side of the company, and normally we would not want to invest in a company that was a one-man operation.

THE COURT: You didn't talk to Hessdorf about their return policies?

THE WITNESS: No.

THE COURT: I am curious why you didn't. It seems to me that is what you would want to know.

THE WITNESS: Well, it wasn't what I really wanted to know at the time. I mean, this -- as I looked at the financial statements of Topper, there was nothing --

THE COURT: But you told me earlier that what troubled you was what protection they were going to have against getting this merchandise back. Orenstein told you they were going to be hard-nosed about it and that they had complete protection. It seems to me these people would want to clear that up in a minute.

THE WITNESS: At the time I thought -- I think it was actually Mr. Rose, the financial vice president -- there wasn't a problem in the company that would relate to returns and there was a legal obligation for the people who took the merchandise to pay for it.

THE COURT:Yes, but couldn't you have found that out, couldn't you have checked that out by asking these people one question each?

THE WITNESS: Well, I thought I checked it out in two other places later on, one with Glover Johnson, who cited this consignment arrangement that they had been abandoned, and then in a meeting on September 1st with Orenstein and others from Topper ~~M~~management he assured Mr. Mole and I that this program had been eliminated.

I asked the toy buyers there where the relationship was satisfactory there and I thought that this would be the kind of thing that they would tell me here if they were going to open up to me and they in fact I think characterized it as being -- Dawn as being a very successful program and never mentioned anything about the right to return Mattel's Hot~~e~~ Wheels. In fact, the implication was they were stuck with them and this was why they were mad.

Q You referred in your colloquy with his Honor I think to a telephone conversation with Glover Johnson.

A That is correct.

Q Would you look at Plaintiffs' Exhibit 1377 before you. Is that a memorandum you dictated shortly after your telephone conversation with Glover Johnson?

A Correct.

Q And that memorandum is August 12th, is it, 1971?

A It is.

Q Could you state the substance of that conversation?

A Well, the two things that I most wanted from Glover Johnson was a check on the integrity of management from somebody that I felt was like the people in the Pension Fund and who knew us well and as a partner of White & Case was an honorable man himself.

THE COURT: White & Case represents U.S. Steel, doesn't it?

MR. BICKS: Right.

THE WITNESS: They do, and they also had been -- I guess done a lot of the legal work, if not all of it, in terms of the private placement purchase agreements that the Pension Fund had done over the years.

A And then the second point was to get some background on the past history of Topper and how a company that had had the losses that it had could be a suitable investment for a pension fund.

Q Mr. Thompson, before you go off on that, just so your response to the Court's question is clear, had Mr. Johnson ever done any legal work for the Pension Fund, to your knowledge?

A To my knowledge, no.

Q You were going on to state the substance of your conversation with Mr. Johnson.

A Yes. My question to Mr. Johnson was how he became involved with Topper and he indicated that he had become involved with it in the buy-back from Philadelphia & Reading and that Topper had gotten in trouble in the past when the chief executive of Philadelphia & Reading had forced the company to ship out merchandise in December so that he could take the profits from those sales, which were recorded, I gather, from the December year into the earnings of Philadelphia & Reading and in effect manipulated the earnings for the year at a time when he wanted to do this.

May I state that over?

THE COURT: Sure.

A What they were doing was shipping out merchandise in December, recording that as sales and profits in the year ending December 31st. This raised the earnings of Philadelphia & Reading in that year and in effect resulted in a manipulation of earnings of Philadelphia &

Reading.

Mr. Johnson said that Henry Orenstein wanted that consignment/ selling, as we referred to, stopped, and he said that this was the reason that Orenstein had wanted to buy back Topper from Philadelphia & Reading.

He felt that Orenstein -- excuse me -- he said that Orenstein felt that he either had to leave this Philadelphia & Reading organization and found another toy company or else arrange a buy-back here and Mr. Johnson felt that the more honorable thing was for Orenstein to buy back the company and he cited -- he definitely said the practice of selling on consignment had ended and this was the principal reason he gave for Topper coming out of Philadelphia & Reading.

This second point related to Orenstein's integrity and he said that he was honest and hard working and gave a brief description of his background.

Q You testified as to your two trade checks with Zayre and Penney, your conversation with Mr. ~~Cerp~~ Cerf, your conversation with Mr. Johnson.

Do you recall anything else that occurred during this period of Mr. Mole's holiday? Did you in fact meet, for example, with Topper management again?

MR. WOLLEN: Your Honor, just so the record is clear, I think Mr. Thompson also referred to a conversation with a Mr. Schwartz.

MR. BICKS: Yes.

MR. WOLLEN: Which you did not just include in your summary question.

THE COURT: Put in Schwartz.

MR. BICKS: Yes. I simply want to ask him did he do anything else.

A Well, I talked with Schwartz, which I mentioned before, and then I had this meeting on the 13th with Downs and Rose.

Q Would you tell the Court what happened at that meeting?

A Well, Mr. Mole was on vacation and Mr. Harrison was the only one of the two vice presidents in the office, so Mr. Harrison and I met with Mr. Downs and Rose. In this meeting Downs described the growth in the toy industry and the fact that the larger companies, such as Topper, were getting an increasing share of the business. He told me that this Dawn program was successful and I believe mentioned that they had reordered merchandise. He actually brought in the brochure I think that they had sent out to the trade the year before on the Dawn program and he indicated they were going to do a similar program the end of

1971.

We discussed the importance of Henry Orenstein in the situation as this appeared to be a substantial negative in the company.

THE COURT: Negative only because you didn't want to rely on one man.

THE WITNESS: Right.

A He said that the trade viewed the company as it had been a year or so ago, when in fact Orenstein did dominate the marketing side of it, but that they now had Orenstein in more of a supervisory role, but still contacting important clients like Korvette's or Vornado, Two Guys from Harrison. They now had brought in Jack Jones to be in charge of promotion and he mentioned a man named Mr. Pierce, whom I had not met, who was in charge I believe of sales, and they did a good job of indicating that the management had broadened out under Orenstein, that he was becoming much more of a supervisor than he had been in the past ~~where~~ when he was really the order taker and supervisor together.

THE COURT: I gather from yesterday's witnesses it wouldn't have made much difference how many people he had around him, Orenstein would still be running the show.

THE WITNESS: That is what we had concerned ourselves about going into the interview and they convinced us that that was not the case. The part of this meeting that we spent the most time on was reviewing a booklet called "Examples of the Company's Reporting."

Q On that point, Mr. Thompson, do you have before you the docment marked as Plaintiffs' Exhibit 1459?

A Yes, I do.

Q Is that the Examples of the Company's Reporting that was given to you on Friday the 13th, by Mr. Rose and Mr. Downs?

A Yes.

Q You have before you, Mr. Thompson, a document marked as Plaintiffs' Exhibit 1378, which appears to be a memorandum from you to Mr. Mole dated August 17, 1971. Is that a memorandum you wrote shortly after your August 13th conference with Mr. Rose and Mr. Downs?

A It is.

Q That is a copy of the memorandum you dictated shortly after the meeting?

A Yes, it is.

Q Do you have it before you?

A I do.

Q I call your attention to the last paragraph on the first page and the last sentence thereof on the first page that reads:

"The only real negative in the company's present financial position is the 13 to 14 percent interest rates that it is paying on its bank lines and the Ford Credit issue, but the company has a 100 percent markup on cost for many of its toys so that it can afford to pay this rate."

Was that rate the subject of discussion at your 13th meeting?

A No, it wasn't. This was a point that Mr. Mole wanted me to check out out later on in our investigation with First National City Bank to see whether this indicated a unusual degree of risk in Topper.

Q Following your meeting --

THE COURT: Wait a minute. You say it was not a point of discussion?

MR. BICKS: No.

THE COURT: Then how did you happen to put it in the memorandum?

THE WITNESS: What happened was I believe that that was mentioned in the original Private Placement Memorandum that came from Hayden Stone as a footnote.

THE COURT: I am puzzled. This is a meeting with David Downs, so and so, and this purports to be what transpired at that meeting and you have a sentence in here and you say that didn't transpire then.

THE WITNESS: Well, it was --

MR. BICKS: Sir, I think if you read the memo, he reports what transpired and then makes his own comments as a guide to Mr. Mole as to where they go from there.

THE WITNESS: The flavor of these is that we are writing these memoranda, Mr. Mole reads them and then reacts to them on the same or very shortly thereafter, after receiving it.

THE COURT: I don't see why it is particularly significant whether that was discussed or not.

MR. BICKS: No.

Q Before we leave the week ending Friday the 13th, you did testify that you had a telephone conversation with Mr. Schwartz of Burnham & Company?

A That is correct.

Q Prior to your conversation with Mr. Schwartz were you aware of his status as a toy security analyst?

A Yes, I was. I had met Mr. Schwartz.

Q Could you describe the circumstances under which you became aware of his status?

A Well, Mr. Schwartz, I believe, was then a young man in his mid to late twenties and he had hosted a meeting

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some time before the private placement for the management of Mattel and I had attended that meeting and also he was writing periodically reports recommending the stock of Mattel. I think he also had a few recommendations on Ideal Toy Company, but he was really -- identified very closely with Mattel.

Q Had Mr. Orenstein prior to your conversation with Mr. Schwartz commented on Mr. Schwartz' tie to Mattel?

A Yes, he did.

Q What did he say?

A Well, he felt that any information that he gave Mr. Schwartz would be relayed to Mattel and Mattel was really the arch rival of Topper.

THE COURT: You probably told me who Mr. Schwartz is but I have forgotten.

THE WITNESS: He is a toy analyst at Burnham & Company in his late twenties, mid to late twenties.

THE COURT: Burnham & Company is a securities house?

THE WITNESS: Yes. I think it is now Drexel Burnham.

THE COURT: He didn't work for any toy company, he worked for Burnham.

THE WITNESS: That is right.

Q In light of your reference in the August 7th memo to the rate on Topper's secured lending arrangements, did you have any further conversation with anyone concerning Topper's banking relationships prior to Mr. Mole's return on the 23rd?

A After the meeting with Rose and Downs in one of our conference rooms, I then took them upstairs to luncheon and at that point I asked Mr. Rose what eligible -- excuse me -- I asked Mr. Downs what "eligible receivables" meant and he indicated that they were receivables that were less than 60 days past due, and it came up in the context of whether there was any security that the banks didn't have as collateral for their loan and he said, "They have got everything in the company, they got the machinery, the molds, but the thing they really look to are the accounts receivable."

Q Who is Downs now?

A Downs was executive vice president of Topper and he had been a vice ~~present~~ President of Manufacturers Hanover, I believe, for 14 years before joining Topper.

So they gave me an elaboration beyond what was in the Private Placement Memorandum as to what the bank was really looking to in Topper for its lending.

Q During this period did your have any discussions with anyone else at the Fund concerning the proposed private placement, at the Pension Fund? You have testified as to discussions with those outside the Fund.

A I had a discussion, I believe, between the 16th and the 23rd with a George Nelson.

A Who was Mr. Nelson at that time?

A Well, Mr. Nelson had retired from his position of vice president. He was the one that I went to Beverly Enterprises at Citibank with. But he was a consultant to the Fund, so that he was in effect in a semi-retired status.

Q Right.

A Mr. Nelson had been the one at the Fund that had done most of the private placements and he had been quite successful at it. So I had lunch with him and outlined in general the work that I had done, but this was fairly complete. I told him about the trade checks and I told him about visiting Topper's headquarters and I believe I mentioned the Schwartz conversation and asked if there was anybody on Wall Street that he knew from his years of experience that knew much about the toy business and he didn't ~~blieveg~~ believe that there was.

And then, you know, I told him at this point that we had not checked the current financial condition of the company and that it was dependent on bank financing and that Citibank was the lead lender in be group and I asked him if he thought it was wise to check with them and whether it was appropriate to do it under the investment relationship with Citibank.

Q And what did Mr. Nelson say?

A He said yes, it was, and he thought this was a good idea.

Q And that was a luncheon conversation some time the week beginning the 16th of August, was it?

A That is correct.

Q Just to complete the record, prior to Mr. Mole's return on the 23rd, if I may, you have before you a document introduced in evidence and marked as Plaintiffs' Exhibit 1380, which appears to be a letter addressed to you by Mr. Jack J. Rose bearing the date August 18, 1971.

Could you describe the circumstances under which that letter came to be sent to you, if you know them?

A In this meeting with Rose and Downs on the 13th I had asked them for any later firm statements that came out after the June figures that were in this "Examples of Company's Reporting" here and I also asked them to prepare for me a failsafe calculation to indicate at what level Topper could operate and meet the interest payments and sinking fund payments if they knew it was going to be a toy year -- a bad toy year ahead of time. In other words, what I was looking for was to see if they could adjust their cost structure and whether there was enough flexibility in the operation so that they would be able to continue in business successfully if it were a bad toy season.

In response to that he sent me this document.

THE COURT: I am still puzzled why you say that you didn't discuss interest rates with him at that meeting and here there is a letter that starts off talking about interest rates. I don't see what difference it makes whether he discussed interest rates or not, but --

MR.BICKS: No, no. Sir, if I can straighten it out, the quote was the rate paid the banks. The letter deals with the total amount the company must earn to meet its charges.

THE COURT: Its interest charges?

MR.BICKS: Yes.

THE COURT: There is no other interest except at the bank?

MR.BICKS: Right, sir.

THE COURT: It is probably an irrelevant confusion, but --

THE WITNESS: This was a pro forma calculation to reflect the interest on the Private ~~paleement~~ Placement and also interest on the Ford Motor credit arrangement that was going -- that I had been told was going to close before the end of August. So these would be the additional interest --

THE COURT: I see. Beside that.

THE WITNESS Beside that.

(Continued on next page.)

Q Can you recall anything in addition to what you have testified to which you regard as important in that period, that is, the period of Mr. Mole's holiday from approximately August 6 to August 23 in connection with Topper?

A I don't recall anything.

Q Following Mr. Mole's return on the 23rd did you have a discussion with him concerning steps you had taken in his absence?

A Yes, I did. I gave Mr. Mole the memoranda that I had prepared on Topper, I think, sometime either late Monday afternoon on the 23rd or early on the 24th. He read the memoranda and then came and we discussed the Topper situation. Then at this point, you know, I told him, "We really have not made a check of the company's current financial condition at the moment, and the Ford Credit loan is going to be at 13 or 14 percent."

I pointed that out to him in this memorandum of the 17th and asked him if it was really appropriate to check with the First National City Bank under our investment advisory agreement.

Q What did Mr. Mole say?

A Mr. Mole said, "Yes, we pay these fellows hard cash and it is perfectly all right to do so."

Q Will you carry on your conversation with Mr. Mole on the subject?

A I then asked Mr. Mole what was the best way of approaching the bank in order to get the maximum help in evaluating whether to make an investment in Topper, and he said, "You go through Walter Jeffers; he is the fellow who coordinates First National City Bank with the Pension Fund."

Q Did you, in fact, contact Mr. Walter Jeffers?

A I contacted Walter Jeffers within a day of August 25, I believe.

Q How did you contact Mr. Jeffers?

A I telephoned Mr. Jeffers.

Q What did you say to Mr. Jeffers?

A Well, I told Mr. Jeffers that we were considering making an investment in Topper convertible debentures; I told him that Mr. Mole had suggested that I call him; and I also reminded him that I had met him earlier in the spring of 1971 at one of these investment meetings with the bank people, just to be sure he knew who I was.

I then told him that I had been out at Topper's headquarters and that I had questioned the company about its banking relationship and with particular emphasis on the accounts receivable and inventories and had been told that Citibank was the lead bank in the lending group for the company. And then I asked him for whatever help the bank could give us in evaluating whether to make an investment in Topper.

Q What did Jeffers say?

A Well, Jeffers had never heard of Topper before.

Q Did he say that?

A He did say that. He asked me to repeat the name of the company, and I told him it was Topper, and I told him it was a toy company and that the financing was in the secured part of the bank.

Q In the course of your conversations with Mr. Jeffers, did you ever mention the name of any bank officer?

A No. I just would not have done that with Jeffers or anybody else in making this kind of a check, because I wanted him really to go to whomever in his organization could be the most help to us in evaluating it and get back to me.

Now, as a practical point, Mr. Orenstein had told me that Waldman was the senior man on this account and I would have had to have an input of some Waldman or somebody very familiar with his work as to what was going on in this financing arrangement, with respect to the current financial condition of Topper, because that is what Mr. Mole was interested in.

Q My question was, did you mention the name of any other officers to Mr. Jeffers?

A No.

THE COURT: The financing was in the secured part of the bank, you were told?

THE WITNESS: That is correct.

THE COURT: You knew that?

THE WITNESS: That is correct.

Q Did Mr. Jeffers ask you any questions during the course of that conversation?

A I don't remember. I think he took down my telephone number, which is an inside number, a Centrex number there, and I think he said somebody in the bank would get back to me.

THE COURT: He didn't tell you he didn't know anything, but he indicated that by the questions he asked you?

THE WITNESS: I think he told me he never heard of Topper before and he asked me to repeat the name of the company.

THE COURT: In answer to Mr. Bicks' question you said you didn't know. Mr. Bicks asked you that question.

You said no, he didn't say that, but that you gathered it. I don't think it is particularly important.

THE WITNESS: I know I had to give him the name Topper twice in here and make sure that he had the right company that I was checking.

THE COURT: By whatever device, you acquired the impression that he had never heard of it?

THE WITNESS: That is right.

Q How did the conversation with Mr. Jeffers end?

A He said somebody would get back to me that would be of help in evaluating the situation.

Q Did somebody from Citibank get back to you?

A Yes.

Q Prior to somebody from Citibank getting back to you, did you take steps to in any way prepare what questions you were going to put to whoever got back to you?

A Well, before calling Mr. Jeffers I had written out on a yellow sheet of paper about so high (indicating) a list of about ten questions, and these included specific reference to the two points I discussed with Mr. Mole and a number of others, and left room on that to write down any comments. I put this aside because I really didn't know when somebody was going to call me from the bank, as to whether it was going to be an hour or so afterwards, and I wanted to be prepared to either talk to him over the phone or meet with him, if that is what he wanted to do.

Q So you had this list of questions on a yellow pad in front of you?

A Yes.

Q Did you have that yellow pad in front of you when you talked to Mr. Jeffers?

A I believe I did. I had it to one side there, but I really didn't expect Mr. Jeffers to know anything about Topper; I thought he would have to go to somebody else in the bank.

Q And you indicated, I believe, that someone else in the bank did contact you following your request of Mr. Jeffers?

A Well, Mr. Waldman called me up on the afternoon of Friday, the 27th, I think sometime approximately 3 o'clock, and he said he was replying to Jeffers' request to call me. And I told him I was an investment manager at the Pension Fund and that we were considering making an investment in the Topper Private Placement, and I told him that we had no experience in investing in the toy industry.

Q What did he say to that?

A I don't really remember what he said specifically, but the thrust of it was that I could go ahead and ask my questions on the pad, "I will be of whatever help to you I can."

Q What was the first question you asked him?

A Well, the first question was, "What is the current size of the loan with First National City Bank?" And I had put this in really as an introductory question, which I thought he would be able to answer easily and would set the stage, really, for a good interview; in other words, I did not want to antagonize him by asking him a question he could not answer at the start of the interview. And he replied to that, "Several million dollars."

He then went on to add that Citibank held, I believe a 40 percent participation in the overall bank loan and was lending up to 80 percent of the eligible receivables.

Q Did he explain what was meant by "eligible receivables"?

A No, he did not. I knew that from the ~~Down's~~ DOWNS luncheon conversation.

Q What did you understand eligible receivables to mean from the ~~Down's~~ DOWNS luncheon conversation?

A That these were receivables that were less than 60 days overdue.

Q Is that your sum total of what constituted eligible receivables?

A That is right.

Q What about "ineligible receivables"?

A I don't think we ever discussed "ineligible receivables".

Q What was your next question of Mr. Waldman?

A The next question was, really, the one that came up in the discussion with Mr. Mole, where I had pointed out in the memo of the 13 percent lending rate, and so I asked him, "Why is the lending rate on the Ford Credit agreement so high and why is the lending rate on the secured agreement as high as it is?"

And then he went on to say that Ford Credit in the past had undercharged for a given level of credit worthiness, and that now they were basically charging what the traffic would bear, and in view of Topper's past history they could get 5 1/2 percent over the prime.

I then asked him about the bank lending rate, and he said that that was as high as it was, and I think he said it was 6 percent plus 3.1 percent, which was spelled out in either the Private Placement Memorandum and the Prospectus, and he said that was because the bank performed these extensive, and I think he said time consuming, audits of Topper's receivables.

Q On that point you indicated that the subject of the rate charged by the bank had come up in your discussion with Mr. Mole prior to your having called Mr. Jeffers. Could you be more specific as to how that point seemed significant to Mr. Mole?

A Well, in a rate that high it was an obvious question as to whether this reflected a risk element in Topper, and that was really what I was trying to convey to Mr. Waldman, and Mr. Waldman came back to me not with risk, but, in effect, "It is because we are entitled to get more because we do these audits of receivables and we do a lot of work for the company," and with Ford it was a case of, in effect, taking advantage of the company's past record to charge what the traffic would bear.

Q I believe you ended up with Mr. Waldman referring to the amount of work the bank did in connection with audits and other matters involving Topper. What was the question after that you asked Mr. Waldman?

A Well, the next one was, "How has the company performed in these audits? Are there any problems that you see in the current financial condition of Topper?"

Q Let us stick to the first part of that, "How does the company perform the audits?" What did you mean?

A I really meant what I asked in the second part. I had written down on the paper to specifically ask, you know, what is the current financial condition of Topper, and Waldman's response to my first question led into that second question, and that is what we then discussed.

Then the next category or topic here --

Q Go ahead. In response to your question as to how the company had performed, were there any current financial problems, what did Mr. Waldman say?

A He said there were none. He said, "Nothing showed up in the audit of receivables."

Then I asked him whether the company had good control in the earnings. He said yes, it had. And I wanted to get his judgment of Mr. Rose, and I asked him if he knew him. He said he did. And then I asked him whether he considered Rose to be a competent financial officer, and he said he was considered to be a very competent financial officer.

So the thrust of these questions was to get assurance that, you know, there were no problems that Waldman knew of in the financial condition of the company.

Q Or to learn from him what the problems were, if there were any?

A Exactly.

THE COURT: As I understand it, you were talking to Orenstein and you were specifically concerned with whether or not the purchasers had the ability to send back the stuff.

THE WITNESS: Yes.

THE COURT: Why didn't you ask this man that specific question?

THE WITNESS: I really didn't think that would have been his area.

THE COURT: Why didn't you ask him and find out? You talked to two people who would know, and you inquired of this man and you never asked him that? The only reason I am asking you the question, it raises in my mind this only became important to you subsequently and you are dating back in your own mind -- I am not suggesting you are not being honest in your testimony -- that you are dating back in your own mind a concern which you never had, because I cannot understand how you would have asked trade people these questions which you said were bothering you and not ask this man.

THE WITNESS: I thought from the conversation with Rose that, you know, in effect, it was not a problem in the company.

THE COURT: That is what Rose said. He had an interest. He is trying to ~~tell~~ sell you five million bucks. Now you are checking up on Rose and you come up against three people, two of them who would conclusively have information, and the third I would have thought had it, and you didn't ask the question.

THE WITNESS: Well, I had gotten assurance from Glover Johnson --

THE COURT: Glover Johnson would not know about it? He might or might not.

THE WITNESS: He might.

THE COURT: But this man clearly would. I am just raising this here because it raises to me the question -- and we all do this -- I am not questioning your honesty -- we all get into a situation where in the past we wish we had done something, and then after about three weeks wishing we remember having done it.

MR. BICKS: I don't mean to interrupt your colloquy with the witness, I simply point out that you are addressing someone who was in the financial end.

THE COURT: I am just suggesting that he did not consider this important at the time.

MR. BICKS: I think it is important that the issue of returns and consignment in retrospect not be blown out of proportion to what it was at the time.

THE COURT: On direct examination he several times said how important he thought it was. I am just questioning whether he did, in fact, think it that important at the time. Maybe it is not important.

MR. BICKS: It was one of several points covered on at least three different occasions, as the testimony will develop. On the other hand, the point with regard to the situation is that it was with regard to the financial condition of Topper, not with regard to its business practices that Topper was engaged in.

THE COURT: The financial problem with Topper: Were these real sales or not real sales? It seems to me with one question of Mr. Waldman, it would have disposed of that.

MR. BICKS: Assuming an honest response.

THE COURT: Assuming an honest response.

MR. BICKS: So the question asked, is there any problem in terms of Topper's financial condition, picks everything up.

THE COURT: If he had been talking to a widow, that is one thing; he is talking to an expert in finance; it seems to me he can assume the man can answer the questions and not speculate.

MR. BICKS: As to Topper's current financial condition.

THE COURT: I mean Mr. Waldman. I am asked a general question, "Are there any problems?" I may perfectly answer "no," whereas if they ask me, "What about the returnability of these? Is that a problem?" I might very well say, "I don't know if it is a problem or not, but it sure worries me."

MR. BICKS: In an inquiry on Topper's financial condition?

THE COURT: This idea occurred to me when I was reading your brief, long before I got into this. I read the quotation you had twice in your brief, where he said, "I asked him whether there were any problems and waited to see if he would qualify it and he did not qualify it." My reaction was that is the damnedest way I ever heard to get information in my life, to wait to see if he was going to qualify something. He testified it was on his mind whether or not these things were returnable. Why didn't he ask?

MR. BICKS: That was one of the matters on his mind, yes.

THE COURT: He gave the impression on direct that it was the most important matter.

MR. BICKS: This is all in retrospect.

THE COURT: We are all seeing it in retrospect as an important matter. If he didn't think of it as an important matter, then maybe Waldman in good faith would not have thought of it.

MR. BICKS: Bearing in mind that he had before him the Private Placement Memorandum with the information that it contained.

THE COURT: Maybe nobody felt it was important. In retrospect we all know it was important.

I have got to decide, was Waldman being fraudulent in giving these answers?

MR. BICKS: Or did he fail to reveal something that he knew?

THE COURT: And knew was important.

MR. BICKS: That is right, to somebody making an investment.

THE COURT: Which he knew was important.

MR. BICKS: Right.

THE COURT: I am troubled by the fact that this expert did not ask him the question which would have revealed that.

MR. BICKS: Expert in what?

THE COURT: In investments.

MR. BICKS: OK.

THE COURT: This is not a widow.

MR. BICKS: He is not an expert in the toy business.

THE COURT: He is not a widow coming in with a little bag of savings bonds. So the question is, what did Waldman think? And if he didn't think it was important, maybe I should think Waldman did not think it was important.

MR. BICKS: Can we go on with the conversation?

THE COURT: I am revealing my thinking for your benefit. I am not deciding it.

BY MR. BICKS:

Q You asked Mr. Waldman if there were any problems. What was his response?

A Well, I mean I covered these two points that had come up in discussion with Mr. Mole, and I think at that point I asked whether there was any problem that had come up in these audits of receivables.

Q What was Mr. Waldman's response?

A There were no problems in the audits of receivables, and so I covered these two points and then I went on to this general question, "Are there any current problems in Topper?" to which he replied, "No." And I gave a pause and gave him a chance to add any information or to qualify it. And then I went on to ask him, "Do you anticipate any problems in Topper?" And here again he replied, "No." And when I dictated this memorandum, which was right after the conversation, I had this right in front of me and just turned around and put it in the memo. So I thought I had covered two specific points that Mr. Mole had asked about and then opened it up on a general basis, because I had had little experience in the toy business and little experience in dealing with somebody who was in secured loans. This was not something that we usually did. So that, in effect, I was relying on the fellow to be helpful to me in this situation, and I thought I had given him a series of about ten questions, which if he had any inclination to be helpful to me, he had plenty of opportunity to do so. I just don't see how he could say that there were not any problems in the audits of receivables when later on we found --

MR. WOLLEN: Your Honor --

THE COURT: It is all right for him to sum up also.

MR. WOLLEN: Will you take my side, too?

Q I think the last question, you said Mr. Waldman had given ~~him~~ his answer whether there were any problems. What was the next question?

A The next question is what experience his division had with respect to lending to the toy industry, and in this he said that they had experience, but he didn't remember the names of the companies at this time. And I said, "Well, what about Mattel?" He said, well, not in his division of the bank, but maybe elsewhere. And I asked him the same question again, because he had said they had experience, but he had not given me any names. So on this point I really did not rely very heavily on his judgment, but I had another question on this list about if he had any experience as to how he would rate Topper. And I asked him whether he would rate it highly or average or below average. And he indicated highly, but it was with reference to an unknown body of information. The last question here that I had on my list was the importance of Henry Orenstein and his role in the company, and this was in a sense of rehash of information that I had obtained elsewhere and it not that I was primarily interested in talking to Waldman about, but in the course of this he seemed to have a good feel for Topper; in other words, he knew that within the trade they considered Topper very good in estimating the cost of production of a new toy before it actually went into production; in other words, if they thought they were going to do X hundred thousand units, and estimated the cost per unit and came very close to it.

He was aware that Orenstein's pet Sesame Street toy was the Spell-O-Phone, and that others in the company had developed toys which I think we both thought were more interesting, namely, Walking Letters was one that we discussed, and he was also aware that Orenstein was checking with the trade to see how the Dawn program was doing and how the other Topper products were doing, and at this point I asked him if the bank in connection with its audits made any independent checks in the trade to, in effect, confirm what Orenstein was telling them, and he said, yes, they did.

And I asked him whether there were any problems or anything came up in those checks that was negative, and he said nothing came up.

Well, at this point from my perspective of being an investor, I covered, you know, the list of questions, I had done it from the point of view of somebody who had experience in retailing in drugs, but very little experience in toys, and I made that known to Waldman at the start of the conversation. In an effort to see if he had anything else he wanted to add, I said, "Look, we have not had any experience investing in this industry, and, you know, we are a tax free pension fund. If we invest in it, we lose a hundred cents on the dollar and don't offset it with profits from the sale of IBM. Is this a suitable industry from a risk standpoint for us to invest in?" And that is a question that the man did not answer. He said, "I can talk to you about the audits of accounts receivables and from the prospect of a financial man in this area, but I really don't know anything about your portfolio or cash flow and I can't make an investment judgment for you."

Now I honestly don't remember the man's exact words, but that is the thrust of it.

THE COURT: Suppose we take our luncheon recess.

MR. BICKS: Very well. What is your pleasure?

THE COURT: Two o'clock. I trust I am on time, for I have a hearing at a quarter of two in the robing room.

(Luncheon recess)

AFTERNOON SESSION

2:15 p.m.

HENRY L. THOMPSON, resumed.

THE COURT: Sorry to keep you waiting. I just sent those people up to reverse me.

DIRECT EXAMINATION (Continued)

BY MR. BICKS:

Q Mr. Thomson, approximately how long did your conversation with Waldman last?

A It was approximately 15 minutes.

Q Following that conversation did you dictate a memorandum concerning what was said?

A Yes, I did. I dictated it immediately following the conversation from the notes that I had taken during the conversation.

Q You have before you a one-page memorandum addressed to Mr. Mole, signed by yourself, bearing the date August 30, 1971, introduced in evidence as Plaintiffs' Exhibit 1379. Is that a copy of the memorandum to which you have just referred?

A Yes, it is.

Q In addition to that memorandum to Mr. Mole, did you report orally to him on the conversation?

A Yes, I did.

Q Could you tell us what you said and what he said on that occasion?

A Well, after he read the memorandum we talked about Topper and specifically about the check with the bank with reference to the company's financial condition and he felt that this was about the best type of information that we could get for our purposes because we -- he felt the bank would have the information in their hands to alert us to any problems that we would be interested in and that they had an obligation to tell us by virtue of this investment relationship we had with ~~t he~~ the bank.

Q Is that what Mr. Mole said to you on that occasion?

A Yes, it is.

Q About when did that report to Mr. Mole occur, some time on or about August 30th, was it?

A I believe he received it on August 30th.

Q Did the conversation with him about which you just testified occur on or about that same day?

A Yes.

Q In addition to your report to Mr. Mole on the conversation, did you advise anyone else as to the substance of your conversation with Mr. Waldman on August 27th?

A Well, I told Mr. Inglis --

Q Who is Mr. Inglis again?

A He was the vice president from Hayden Stone who was working on the Private Placement for his firm.

Q What did ~~he~~ YOU tell Mr. Inglis?

A Well, I had told Mr. Inglis that before we would make a decision on whether to go ahead with Topper that we would probably make a check with ~~City Bank~~ Citibank and that in addition that we would have a meeting with the management of Topper to give Mr. Mole a chance to meet them.

Inglis called up to find out how the information that I had gotten from the bank turned out and I don't remember the exact details of the conversation because he was asking me questions and I was replying to him, but I did tell him that there weren't any problems in the audits of receivables that the bank was doing and that we had received favorable information from them, that they viewed the company's management as competent and the controls good and that they didn't know of any problems in the situation currently.

Q You told Inglis that when?

A A few days after August 30th. I would place it between August 30th and the end of that week.

Q You referred to two things to be done,